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The Acte Clair in EC Direct Tax Law

Edited by

Ana Paula Dourado

and

Ricardo da Palma Borges

IBFD

IBFD

Visitors' address:
H.J.E. Wenckebachweg 210
1096 AS Amsterdam
The Netherlands

Postal address:
P.O. Box 20237
1000 HE Amsterdam
The Netherlands

Telephone: 31-20-554 0100
Fax: 31-20-622 8658
www.ibfd.org

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PREFACE

One of the most-often quoted sentences must be that the only certain things in this world are death and taxes. For years, however, tax lawyers have done their best to disprove this saying... I am certain (at least as much as one can be certain...) that tax law scholars, and particularly those contributing to this volume, will forgive me this provocation in order to highlight a paradox of tax law which is shared by Community law: both are legal domains where legal certainty is particularly important but where their contexts of application make it particularly difficult to obtain it. If, therefore, tax law and Community law share this existential tension, it is only natural for it to become even more noticeable when the two fields do come into contact. This book is, first of all, a remarkable analysis and discussion of the legal issues arising from the search for certainty in the relationship between Community law and direct tax law. But, secondly, it is a rare in-depth analysis of the *CILFIT* doctrine in action and its demand for legal certainty. The book reviews and discusses the application in the field of direct taxation of the criteria put forward by the European Court of Justice (ECJ) in *CILFIT* for relieving national courts of last instance from the obligation to refer questions of Community law to the Court. It does so by looking both at how the case law of the ECJ in the area of direct taxation fits the *CILFIT* criteria and how such criteria are complied with by national courts. In the process, the book also manages to highlight some of the current challenges faced by the EU judicial system in view of the expansion of EU law and its decentralized application at the national level.

The initial assumption in the book is perhaps so obvious as to be constantly neglected in Community law studies: that Community law is mainly applied through national courts. The few studies that have been made so far indicate, in effect, that the overwhelming majority of Community law cases are decided by national courts without any intervention by the ECJ through the preliminary ruling mechanism. For this reason, it is essential for the effective and uniform application of Community law that national courts behave as effective Community courts, aware of their institutional obligations towards the Community law system and with a knowledge of Community law "in the books" and "in the cases" of the ECJ.

The importance of the role to be played by national courts in the effective application and enforcement of Community law can only increase in view of the foreseeable increase of Community law litigation due to the rapidly

IS IT *ACTE CLAIR*? GENERAL REPORT ON THE ROLE PLAYED BY *CILFIT* IN DIRECT TAXATION

Ana Paula Dourado

1. Introductory remarks

European tax law professors have been meeting with increasing frequency, in order to analyse and discuss the growing body of the European Court of Justice's (hereinafter: the ECJ or the Court) decisions on the compatibility of domestic direct tax law and the EC law.

The number and scope of the decisions on the aforementioned issue is relevant enough to allow and to recommend a systematic analysis of groups of issues, in order to see whether and to what extent national courts of last instance can, under Art. 234 (3) EC Treaty, as interpreted by the Court in the *CILFIT* case[1], decide cases on direct taxation that involve interpretation of EC law without referring them to the ECJ for a preliminary ruling. This analysis is also important, taking into account that the conduct of national courts can lead to state liability in case they do not fulfil their obligation to refer a case under the aforementioned Art. 234 (3) EC Treaty (see the *Köbler* case[2] and point 6 below) and that the previous non-existence of a preliminary ruling on a legal point of law is a requirement for the ECJ to exceptionally restrict the temporal effects of its rulings (see point 5 below and reference to the relevant ECJ case law). In other words, it is important to understand to what extent the *CILFIT* criteria and the existing ECJ case law on direct taxation can provide some pattern of conduct to national courts (and also to the Member States' tax administrations and legislator) and some legal certainty to taxpayers.

In fact, on the one hand, there are many doubts as to whether national courts in the different Member States correctly apply Art. 234 (3) EC Treaty, as the authors in this book illustrate[3]; on the other hand, although the ECJ decisi-

1. ECJ, 6 October 1982, case 283/81, *Srl CILFIT and Gavardo SpA*.
2. ECJ, 30 September 2003, case C-224/01, *Köbler*.
3. Cécile Brokelind, "The Acte Clair Doctrine Arising from the ECJ's Direct Tax Case Law from a Swedish Perspective: Use or Misuse?", point 5, Francisco de Sousa da Câmara, "The Meaning and Scope of the Acte Clair Doctrine Concerning Direct Taxation: The Portuguese Experience and the Establishment of Boundaries", point 6; Francisco Alfredo García Prats, "The Acte Clair Doctrine and the Effective Judicial Protection of EC Law Rights in Direct Tax Matters: The Spanish Case as an Example", points 4-5 ; Georg Kofler,

ons normally refer to the previous case law, thus creating a system of precedent [4], the predictability of the results of the subsequent related cases is not as high as it could be expected to be, which may lead us to the conclusion that unless a case on direct tax issues is identical to a previous one (*acte éclairé* in the sense of *Da Costa*[5]), a national tax court should always refer a case, contrary to what the ECJ recommended in *CILFIT*, in order to avoid inconsistencies regarding the interpretation of the fundamental freedoms (see, for example *ICI*, *Lankhorst-Hohorst*, *De Lasteyrie du Saillant* and *Cadbury Schweppes*, on the one hand, and *Columbus Container*, on the other; *Gerritse*, *Scorpio* and *Centro Equestre da Lezíria Grande*; *Schumacker*, *Geschwind* and *De Groot*, on the one hand, and *Schempp*, on the other; *De Lasteryie du Saillant* and *N.*; *Barbier* and *van Hilten*; *Baars*, *X and Y*, *Cadbury Schweppes*, *ACT Group Litigation*, on the one hand, and *Holböck*, on the other)[6].

Moreover, the interpretation of the ECJ decisions in direct tax law issues is far from being an easy task for tax lawyers, and, besides, the Court is not bound to a *stare decisis* rule, which although allowing it to improve its own case law, leads to a tension between the certainty that would result from the aforementioned rule and the need for an evolution in the ECJ's case law.

The fact that the number of judges in the Court corresponds to the number of the Member States, and therefore has been increasing, together with its organization in different chambers, can also explain some unexpected and unfortunately not so-well justified decisions on matters that have been previously decided by the Court and which could even be considered settled case law (see on the prohibition of the home Member States from hinde-

"Acte Clair, Community Precedent and Direct Taxation in the Austrian Judicial System", points 3.1., 3.2; Pasquale Pistone, "The Search for Objective Standards for the Application of the Acte Clair Doctrine to Direct Taxation (with references to Italian tax law)", point 2.2. ; Dennis Weber/ Frauke Davits, "The Practical Application of the Acte Éclairé and the Acte Clair Doctrine (with References to Netherlands Direct Tax Law)" points 6.2., 6.3. See, also, the papers published in Parts 2 to 6 of *Towards a Homogeneous Direct Tax Law, An Assessment of the Member States' Responses to the ECJ's Case Law* (ed. by Cécile Brokelind), IBFD, Amsterdam, 2007.

4. On this methodology, Paul Craig/Gráinne de Búrca, *EU Law, Text, Cases and Materials*, 4th ed., Oxford, 2008, p. 468 (467 et seq.).

5. ECJ, 27 March 1963, Joined cases 28 to 30-62, *Da Costa en Schaake NV*.

6. See also, on the increasing uncertainty resulting from the ECJ case law on the fundamental freedoms (in general), since the middle of the eighties, Thorsten Kingreen, "Grundfreiheiten", *Europäisches Verfassungsrecht, Theoretische und dogmatische Grundzüge*, Berlin, Heidelberg, 2003, p. 631 et seq.; Trevor C. Hartley, *Constitutional Problems of the European Union*, Oxford and Portland, 1999, p. 66 et seq.

ring the establishment in another Member State of one of their nationals or of a company incorporated under their legislation, *ICI*, *Lankhorst-Hohorst*, *De Lasteyrie du Saillant*, *Marks & Spencer*, *Keller Holding*, *Barbier*, *Centros*[7], *Cadbury Schweppes* on the one hand, and on the other, *Columbus Container*) - not to mention the problems arising from the work overload of the Court, which have been the origin of several academic contributions proposing a reform and of commissions created for the same purpose[8].

Taking into account the regime in force, the final word on the interpretation of EC law belongs to the ECJ (Art. 234 EC Treaty), but in order to exercise that competence, the ECJ depends on referrals being sent to it by the national courts, since it is unavoidable that the national courts interpret, in a first moment, whether the issue is relevant from the perspective of EC law and whether the issue needs to be referred to the ECJ[9]. Even if the non-fulfilment of the national courts' obligations to refer a case to the ECJ can, in principle, lead to the liability of the Member State, the criteria settled by the Court, together with its decision in the *Köbler* case, seem to deny such liability in practice, unless, perhaps, in exceptional situations. If this interpretation of *Köbler* is correct (see point 6 below), then, again, cooperation of the national courts with the ECJ continues to be essential to the compatibility of national direct tax systems with EC law[10].

7. ECJ, 9 March 1999, C-212/97, *Centros*.

8. See, for example J.P. Jacqué and J.H.H. Weiler, "On Road to European Union – A New Judicial Architecture: An Agenda for the Intergovernmental Conference", *Common Market Law Review*, 1990, p. 185 et seq.; «Sur la voie de l'Union européenne, une nouvelle architecture judiciaire », *Revue Trimestrielle de Droit Européen*, 1990, p. 441 et seq.; Walter van Gerven, "The Role and Structure of the European Judiciary Now and in the Future", *European Law Review*, 1996, p. 211 et seq.; Hjalte Rasmussen, "Remedying the crumbling EC judicial system", *Common Market Law Review*, 2000, p. 1071 et seq.; David Edward, "Reform of Article 234 Procedure: The Limits of the Possible", *Judicial Review in European Union Law, Liber Amicorum in Honour of Lord Slynn of Hadley*, (ed. by David O' Keefe, Antonio Bavasso), The Hague, London, Boston, 2000, p. 119 et seq.; Kathryn Hummert, *Neubestimmung der Acte Clair Doktrine im Kooperationverhältnis zwishen EG und Mitgliedstaaten*, Berlin, 2006, 3. Teil, pp. 75-100; Daniel Sarmiento, "Who's Afraid of the Acte Clair Doctrine?", *in this book*, point 6.

9. On the domestic procedural rules that may hinder application of the preliminary ruling procedure, see John Bridge, "Procedural Aspects of the Enforcement of European Community Law through the Legal Systems of the Member States", *European Law Review*, 1984, p. 28 et seq.; David O'Keefe, "Appeals Against an Order to Refer under Article 177 of the EEC Treaty", *European Law Review*, 1984, p. 87 et seq.

10. This is not incompatible with the observation of Takis Tridimas, *The General Principles of EU Law, 2nd.* ed., Oxford, 2006, p. 525, according to whom, Köbler "views the relationship between the ECJ and the national courts as one of hierarchy rather than one of cooperation, since, ultimately, it is for the ECJ to determine whether the breach is "manifest"".

As structured, the preliminary ruling procedure of Art. 234 EC Treaty implies an indirect access of the taxpayers to the fundamental freedoms of the EC Treaty. To what extent an effective access exists, and the degree of homogeneous application of Community law within the European Union in 20 years of the ECJ case law on direct taxation, were the two main questions guiding Brokelind's conference held in Lund in 2006.

The results are not the desirable ones either from the perspective of the effectiveness of ECJ case law or the protection of the taxpayers covered by EC law, as it seems that "the actual impact of the ECJ's case law is not as extensive as it should be" and that "the most adequate way to measure the actual impact of the ECJ's case law on Member States' domestic tax law [is] to analyse domestic judges' attitudes towards this source of Community law"[11].

Further discussion of this topic required the analysis of the meaning and scope of the *acte clair* doctrine in direct tax law, and this was the object and title of a conference held in Lisbon in September 2007.

As we will see among the different contributions to the book, the meaning and scope of the *acte clair* doctrine are very debatable, but the research on this topic provides us interesting paths.

For the Lisbon Conference, different panels corresponding to different issues were organized and a questionnaire based on those issues was drafted, in order to guide the panellists and the papers that are now being published: the sources and standards of the *acte clair* doctrine in direct tax law; identification of the object of the *acte clair* in direct tax issues; the development of an *acte clair* in direct tax issues (when does an *acte clair* occur); the role of the "relevant objective elements apt to justify a restriction to a fundamental freedom or a discriminatory treatment"; the consequences of the *acte clair* doctrine for the national courts and temporal effects of an ECJ decision; damages and liabilities; the interpretation of the *acte clair* doctrine by the courts of the Member States.

The first part of the book includes papers on some of the specific topics discussed in autonomous panels: this is the case for the papers on the meaning of *CILFIT*, on the justifications issue, and on the temporal effects of the *acte clair* doctrine.

11. Cécile Brokelind, "Introduction", *Towards a Homogeneous...*, cit., p. 5.

The other group of papers, published in the second part, answers some of the issues raised in the questionnaire. They contain the authors' perspective on the issue of the meaning and scope of *acte clair* doctrine in direct tax issues and inform us as well about the interpretation of the *acte clair* doctrine by the courts of the respective Member State. This general report follows the structure of the questionnaire and the panels of the conference.

2. Sources and standards of the *acte clair* doctrine

2.1. Paras. 14 and 16 of the *CILFIT* case and Art. 104 (3) of the Rules of Procedure of the Court of Justice

Taking into account its wording, Art. 234(3) EC Treaty contains an unconditional obligation to national courts or tribunals of last instance when a case before them raises an issue of interpretation of the EC Treaty, as they are obliged to refer the issue to the ECJ. In *CILFIT*, the Court considered that national courts of last instance can abstain from referring to the ECJ "where previous decisions of the Court have already dealt with the point of law in question, irrespective of the nature of the proceedings which led to those decisions, even though the questions at issue are not strictly identical" (para. 14) or, it added in para. 16, when "the correct application of Community law may be so obvious as to leave no scope for any reasonable doubt as to the manner in which the question raised is to be resolved" (first part of para. 16).

The ECJ introduces some very restrictive conditions in the second part of para. 16 and paras. 17-20, regarding the consensual interpretation by all potentially competent courts (the national court must be convinced that the matter is equally obvious to the courts of the other Member States and to the ECJ (para. 16)), the characteristic features of Community law (para. 17), the comparison of the different Member States' languages (para. 18), the autonomy of Community law and its concepts (para. 19), the systematic element of interpretation and the state of evolution of Community law at the date on which the relevant provisions are applied (para. 20), all of these aimed at avoiding quick and wrong decisions of national courts not to refer. They are criteria that contribute to diminishing the indeterminacy resulting from the first part of para. 16[12], even if the definition of interpretative doubt

12. Advocate General Stix-Hackl, Opinion delivered on 12 April 2005, case C-495/03, *Intermodal Transports BV*, point 90; See also in this book, Adam Zalasinski, "Acte Clair, Acte Éclairé...", cit., pp. 325-326.

can itself be considered rather "strict"[13]. However, if each of these conditions were taken into account by the national courts, *CILFIT* would only exceptionally admit avoiding of the preliminary ruling procedure created by Art. 234, and what is more, comparison of different Member States' languages not only was interpreted in a narrow way by the Advocates General ("Cilfit cannot be intended to mean that the national court is required...to examine a provision of Community law in every one of the official Community languages"[14]), but it seems as well to have been abandoned by the ECJ in its interpretation methodology[15].

CILFIT was the first mechanism of docket control implemented at the ECJ, in the context of a growing number of preliminary rulings and with a view to the continuous expansion of the Community to new Member States[16].

The literature usually stresses that para. 14 of *CILFIT* contains a precedent rule (*acte éclairé*) whereas para. 16 of *CILFIT* contains the *acte clair* doctrine, as according to para. 16 no referral is needed, even without a prior ECJ decision on the point[17].

13. Advocate General Stix-Hackl, Opinion on *Intermodal Transports BV*, point 91.
14. Advocate General Stix-Hackl, Opinion on *Intermodal Transports BV*, point 99; cf. Advocate General Jacobs, Opinion delivered on 10 July 1997, case C-338/95, *Wiener S.I. GmbH*, point 65 and Advocate General Tizzano, Opinion delivered on 21 February 2002, Case C-99/00, *Lyckeskog*, point 75.
15. See Advocate General Ruiz-Jarabo Colomer, Opinion delivered on 30 June 2005, case C-461/03, *Gaston Schul Douane-Expediteur BV,* point 58; Pasquale Pistone, "The Search for Objective Standards...", cit., pp. 230-231. See also Francis G Jacobs, "Approaches to Interpretation in a Plurilingual Legal System", *A True European, Essays for Judge David Edward, Mark Hoskins, William Robinson* (eds.), Oxford and Portland, 2003, pp. 303-305. On the fulfilment of the requirement of comparison of languages by the German Courts, see Isabel Schübel-Pfister, *Sprache und Gemeinschaftsrecht, Die Auslegung der mehrsprachig verbindlichen Rechtstexte durch den Europäische Gerichtshof,* Berlin, 2004, pp. 324-332.
16. See, in this book, Daniel Sarmiento, "Who's Afraid...?", cit., p 72. ; see the reference to *CILFIT* as the most practical and objective filter system, on the basis of the EC Treaty, for questions of interpretation to be referred to the ECJ, in Advocate General Stix-Hackl, Opinion on *Intermodal Transports BV*, point 104.
17. Among many, see Paul Craig/Gráinne de Búrca, *EU Law*...cit., pp. 477-478; Jean Paul Jacqué, *Droit Institutionnel de L'Union Européenne,* 2. ed., Paris, 2003, pp. 683-684; Federico Mancini, "L'Art. 177 del Trattato CEE e la Cooperazione tra le Giurisdizioni Nazionali e la Corte", *Diritto Comunitario e Diritto Interno, Quaderni del Consiglio Superiore della Magistratura,* 1987, p. 50; Charlotte Gaitanides, "Art. 234", *Vertrag über die Europäische Union und Vertrag zur Gründung der Europäische Gemeinschaft, Kommentar,* von der Groeben/Schwarze (Hrsg.), Nommos, Band 4., Art. 189-314 EGV, 6. Auflage, Baden-Baden, 2004, p. 544, point 63; Katharina Hummert, *Neubestimmung der Acte Clair...*, cit., p. 34; See also, Advocate General Stix-Hackl, Opinion on *Intermodal Transports BV*, point 74.

Most of the authors in this book expressly accept that distinction[18]. However, if we reject the assertion "*in claris non fit interpretatio*", and take into account that the Court is not bound to a *stare decisis* rule, and also that interpretation is an unavoidable activity that contributes to progressive clarification of the meaning of law, it should instead be stressed that paras. 14 and 16 of *CILFIT* are very much interrelated and the analysis in the papers published here also reflects that close relation between *acte éclairé* and *acte clair*[19].

In direct tax law issues, considering that the Court interprets Community law principles (i.e. the fundamental freedoms provisions in the EC Treaty), which by their nature are indeterminate, it is hard to think of an *acte clair* without previous ECJ decisions on a point of law connected to the one that is subject to analysis (see, for example *Mertens*, which was decided by reasoned order of the Court, and mentioned by Weber/Davits as a direct tax case decided on the basis of *CILFIT*, para. 16, whereas Kofler considers that it was decided on the basis of settled case law; and see also the Austrian tax courts' decisions not to refer, described by Kofler, based on a "no doubt reasoning" which in turn derives from previous ECJ case law[20]). We could then say that *acte clair* presupposes in direct tax law, at least, some degree of *acte éclairé*, and therefore both paras. 16 and 14 will be taken into account by the competent courts.

But in turn, an acte is éclairé under *CILFIT*, para. 14, if it also passes the test of the first part of para. 16, i.e. if it leaves "no scope for any reasonable doubt as to the manner in which the question raised is to be resolved": in other words, contrary to what the first impression may be, due to the fact that there is no *stare decisis* rule, the conditions in para. 14 are not less strict than the ones in paras. 16-20 (there is settled case law if the conditions in paras. 16-20 are fulfilled).

18. Francisco Alfredo García Prats, The Acte Clair Doctrine ...", cit., p. 419 et seq.; Georg Kofler, "Acte Clair, Community Precedent...", cit., p. 177 et seq.; Dennis Weber/Frauke Davits, "The Practical Application...", cit., points 2.2.2., 2.2.3.; Frans Vanistendael, "Consequences of The Acte Clair Doctrine for the National Courts and Temporal Effects of an ECJ Decision", pp. 157-160, 166-168; Adam Zalasinski, "Acte Clair, Acte Éclairé...", cit., pp. 321-325.
19. That is the case of Pasquale Pistone, "The Search for Objective Standards...", cit., point 2.1. ; but indirectly also, Dennis Weber/ Frauke Davits, The Practical Application...", cit., points 4., 6.; Georg Kofler "Acte Clair, Community Precedent...", cit., point 3.; and Cécile Brokelind "The Acte Clair Doctrine...", cit., point 3.1.
20. Dennis Weber/ Frauke Davits, "The Practical Application...", cit., p. 294; Georg Kofler "Acte Clair, Community Precedent...", cit., p. 190.

Moreover, according to Art. 104 para. 3 of the Rules of Procedure of the Court of Justice, the ECJ may, in simplified proceedings, give its decision on a question referred for a preliminary ruling by reasoned order. It is a mechanism of docket control, therefore aiming at relieving the ECJ, upon its own evaluation, of some of its work overload, in case the *CILFIT* conditions are met, although it has seldom been used in direct tax issues (*Mertens, De Baeck, Lasertec, A and B, Stahlwerk Ergste Westig GmbH The Test Claimants in the CFC*) [21].

Art. 104 para. 3 also illustrates that there is a close relation and a quantitative difference between *acte éclairé* and *acte clair*, even though it seems to accept a (qualitative) difference between para. 14 and para. 16 in *CILFIT*. In fact, Art. 104 para. 3 (1) provides that "the Court may also give its decision by reasoned order where a question referred to the Court for a preliminary ruling is identical to a question on which the Court has already ruled, or where the answer to such a question may be clearly deduced from existing case law" (see, e.g. the issue in the origin of the *Köbler* case). And according to Art. 104 para. 3 (2), a decision by reasoned order may occur where "the answer to the question referred to the Court for a preliminary ruling admits of no reasonable doubt". If the answer to a question that, although not being identical to a previous one on which the Court has already ruled, *can be clearly deduced* from existing case law, this then means that there is no reasonable doubt on the issue.

Although it is possible that in the situation foreseen in para. 3 (2) there is no previous case law, the extent to and the manner in which the previous case law is related to the issue under analysis, and even whether it is at all related, can be very controversial in the concrete case (see, e.g. *Verkooijen*, *Manninen* and *Meilicke*; or *Marks & Spencer* and *Rewe Zentral Finanz*; *Cadbury Schweppes* and the Opinion of the Advocate General in *Columbus Container*[22] and the ECJ's decision in that case; *Lenz* and *Holböck*).

Thus, although the difference between the concepts of *acte éclairé* and *acte clair* can be useful, in order to highlight that the main danger of *CILFIT* lies in its para. 16, because it gives a broader competence to national courts in respect of EC law interpretation and because it may be dangerously misinterpreted by the national courts, that differentiation is not of significance

21. See in this book, for example Georg Kofler, "Acte Clair, Community Precedent…", cit., pp. 189-189; Adam Zalasinski, "Acte Clair, Acte Éclairé…", pp. 334-335; Dennis Weber/ Frauke Davits, "The Practical Application…", cit., pp. 282-283; Advocate General Sitx-Hackl, Opinion on *Intermodal Transports BV*, point 106.
22. Advocate General Mengozzi, Opinion delivered on 29 March 2007, Case C-298/05, *Columbus Container.*

from the point of view of the corresponding obligations to refer of the national courts or tribunals, since in direct tax law issues paras. 14 and 16 will normally have to be jointly taken into account. Pistone's paper and the table he proposes for declaring a tax *acte clair* also goes in this direction[23]. In the following pages I will therefore consider that direct tax cases submitted to national courts on legal points that have already been dealt with by the ECJ, but containing "not strictly identical questions to the one that is being analysed" (para. 14) are also subject to the *CILFIT* tests of para. 16 (and 17 to 20), and will accept a concept of *acte clair* that covers the *CILFIT* tests in para. 14 and para. 16 (and 17 to 20), including in it the *acte éclairé*. Whenever the separation between the concepts of *acte éclairé* s.s. (para. 14 *CILFIT*) and *acte clair* s.s. (para. 16 *CILFIT*) contributes to a better understanding of a reasoning I will accept the distinction.

2.2. Who is afraid of the *acte clair* doctrine?

The literature commenting on and interpreting the meaning of *CILFIT* has been divided in two groups: one that stresses the importance of the first part of para. 16 of the ruling, and therefore considers that *CILFIT* basically has a decentralization aim (or effect) [24], and another one that concentrates on the conditions laid by the Court in the second part of para. 16 and paras. 17 to 20, and on that basis argues that the true aim of *CILFIT* is to centralize in the ECJ the competence for interpretation of EC Treaty[25]. The authors that have contributed to this book cannot be so clearly divided into these two groups, as they do not seem too critical of *CILFIT* itself (except for Sarmiento who argues that the *CILFIT* strategy has proven unsuccessful from a federalization perspective)[26], but instead are not satisfied with the way their national courts wrongly apply *CILFIT*.

23. Pasquale Pistone, "The Search for Objective Standards…", cit. pp. 228-229.
24. See on the discussion, Daniel Sarmiento, "Who's Afraid…?", cit., pp. 72-73; and, for example Paul Craig/Gráinne de Búrca, *EU Law…*,cit., pp. 478-479; Anthony Arnull, "The Use and Abuse of Art. 177 EEC", *Modern Law Review*, 1989, p. 626; "Article 177 and the Retreat from Van Duyn", *European Law Review*, 1983, n. 6, pp. 365 et seq.; Ulrich Haltern, *Europarecht, Dogmatik im Kontext*, 2. Auflage, Tübingen, 2007, 237 et seq. 250 et seq.
25. Gerhard Bebr "The Rambling Ghost of 'Cohn Bendit': *Acte clair* and the Court of Justice" *Common Market Law Review*, 1983, pp. 439 et seq. (p. 466 et seq. and p. 471); Haltje Rasmussen "The European Court's Acte Clair Strategy in Cilfit (Or: *Acte clair*, of course! but what does it mean?)" *European Law Review*, 1984, p. 342 (p. 256 et seq.); "Remedying the Crumbling…", cit., pp. 1008 et seq.; Manzini/Keeling "From Cilfit to ERT: The Constitutional Challenge facing the European Court", *Yearbook of European Law*, 1991, p. 1 et seq.
26. "Who's Afraid…?", cit., p. 76.

The ambiguity of *CILFIT* lies in the fact that both readings of the judgment are possible, and the main danger of the *acte clair* doctrine, lies in its *body and soul,* to use the expression of Sarmiento[27]. In other words, the danger lies in the assertion that national courts can abstain from referring an interpretation issue to the ECJ even without previous case law on a similar (not identical) issue, and therefore be the final judges on interpretation of EC Treaty and of whether *acte clair* exists. In this case, divergences among judicial decisions on the interpretation of EC Treaty will occur and the creation of an integrated area will fail. Art. 234(3), as interpreted by *CILFIT*, plays a role that goes far beyond the mere hierarchy of courts, but is a core mechanism for strengthening the Community and its federal elements, for increasing the scope and effectiveness of EC Treaty and promoting European integration. The different Opinions of the Advocates General on the *CILFIT* criteria express these worries, independently of recommendations for self-restraint of the ECJ and the national courts[28], or of attempts to mainly try to reduce the vagueness of the *CILFIT* criteria while nevertheless strongly upholding the *CILFIT* doctrine[29].

Were the national courts ready to cooperate with the ECJ[30], and accept the primacy and direct effect of EC law, the substance of the *CILFIT* doctrine would be highly reasonable. National courts, together with the ECJ, must play a decisive role in interpreting and clarifying the meaning of the EC law, and the ECJ should not be overloaded with issues that have been solved before or the answer to which can be deduced from previous case law, unless there is a reasonable doubt.

Literal interpretation of Art. 234 (3) EC Treaty is therefore not the correct one, and the existence of a *reasonable doubt* is the relevant condition that justifies a referral to the ECJ[31]. In fact, when a decision is not convincing – when there is a reasonable doubt – referrals to courts occur even if a very

27. "Who's Afraid...?", cit., p. 72.
28. Advocate General Jacobs, Opinion on *Wiener,* C-338/95, points. 20-21; Advocate General Ruiz-Jarabo Colomer, Opinion on *Gaston Schul* (C-461/03), point 58 (interpretation less strict of the decision would answer the necessities of cooperation between national courts and the ECJ); point 59 (Limit the referrals to aspects of general importance).
29. Advocate General Tizzano, Opinion on *Lyckeskog* (C-99/00), point 21 (More systematic approach, objective criteria for coherence); Advocate General Stix-Hackl, Opinion on *Intermodal Transports BV*, points 76-108.
30. On the unavoidability of such cooperation, see. e.g. Anthony Arnull, *The European Union and its Court of Justice,* 2nd. ed., Oxford, 2006, p. 98 et seq.; J.H.H. Weiler, *The Constitution of Europe*, Cambridge, 1999, pp. 32-33 and 195 et seq.
31. See Anthony Arnull, "The Use and Abuse...", cit., pp. 622-623; Kathryn Hummert, *Neubestimmung der Acte Clair...*, cit., pp. 101-107, 111 et seq..

similar case has been decided before[32]. The dynamic interpretation of Community law ("the state of evolution of Community law") is of major importance in the application of Art. 234 (3) EC Treaty by the national courts, as the Court held in para. 20 of *CILFIT,* and also in direct tax issues, as Weber/Davits highlight in their paper[33]. It should be added that the filter system of Art. 104 (3) of the Rules of Procedure of the Court of Justice does not avoid the necessity of trusting the judgment of national courts[34].

In this respect, it is important to stress that I do not accept as valid the difference, according to which the ECJ exclusively interpreted Community law, whereas the national courts would apply the decision to the concrete case[35], because the interpretation of the EC law by the ECJ depends on the way national courts present to it the circumstances of the case and the relevant national law – thus both the ECJ and the national courts interpret, to a certain extent, EC law as well as national law in light of the EC law. Moreover, the more detailed is the information given by the national court, and the decision of the ECJ, the closer the preliminary ruling approximates to the so-called application by the national courts[36].

It is true that although exercising a function similar to that of a constitutional court, the ECJ may not have access to all relevant details in order to interpret their compatibility with EC law, which means that domestic law and the circumstances of the case are mainly to be interpreted by the national courts, as the ECJ unavoidably has a limited knowledge of each Member State's legal system. But this is an issue regarding the advantages of self-re-

32. See, for direct tax issues, Pasquale Pistone, "The Search for Objective Standards...", cit..., p. 223-224.
33. See, Dennis Weber/ Frauke Davits, "The Practical Application...", cit., points 2.2.3.; 4.3.2. d), 6.2.2. b); 6.2.3. b); and on the issue in general, and referring to the ECJ relevant case law, see Kathryn Hummert, *Neubestimmung der Acte Clair...*, cit., p. 111 et seq.
34. Advocate General Stix-Hackl, Opinion on *Intermodal Transports BV*, points 106-107. See also, in this book, Georg Kofler, "Acte Clair, Community Precedent...", cit., pp. 188-189.
35. Cf., in the opposite sense, Charlotte Gaitanides, "Art. 234"..., cit., p. 533 (paras. 27-28); Klaus-Dieter Borchardt, *Die rechtlichen Grundlagen der Europäischen Union,* 3rd. ed., Heidelberg, 2006, pp. 261-262 (paras. 637-638); Ulrich Haltern, *Europarecht,* cit., p. 189 (although concluding that often the ECJ goes beyond the interpretation of EC law (pp. 191-192); Schermers/Waelbroeck, *Judicial Protection in the European Communities,* 5th ed., Deventer, Boston, 1992, pp. 384-385. Concluding that "the dividing line between interpretation and application can be perilously thin", Paul Craig/Gráinne de Búrca, *EU Law...*, cit., p. 493.
36. Paul Craig/Gráinne de Búrca, *EU Law...*, cit., p. 493; cf. on the refusal of the ECJ to render a ruling on general or hypothetical questions: Henry G. Schermers/Denis F. Waelbroeck, *Judicial Protection...*, cit., pp. 396-397 (para. 691); Richard Gordon QC, *EC Law in Judicial Review,* Oxford, 2007, points 4.58-4.62.

straint of both the ECJ and the national courts, i.e. of whether "increasing the refinement of the case-law is likely to lead to less legal certainty rather than to more", as Advocate General Jacobs argued (point 21 of the Opinion in *Wiener*)[37].

In its interpretation task, searching for the purpose of the Treaty principles and rules, it is for the ECJ to progressively reduce their vagueness, and to develop its own interpretative principles of EC law[38] – EU integration is a process of construction of principles[39] (the general principle of abuse, for example as an interpretative principle developed by the ECJ[40], goes in this direction).

If we consider the cooperation between national courts and the ECJ in tax issues, it is interesting to verify that whereas self-restraint of the national courts has been recommended in cases of classification of products for the purpose of common customs tariff, and national courts in Member States like Italy and Portugal have been increasingly referring to the ECJ tax issues that are harmonized[41], there is much more reluctance from the courts of these Member States about referring cases regarding non-harmonized direct tax law. And yet, in the absence of comprehensive direct tax harmonization, application of the *CILFIT* criteria in direct tax issues involves interpretation of the EC fundamental freedoms – "the 'support columns' on which the economic constitution of the Community rests" [42] – which, due to their inherent vagueness demands *constructive* interpretation by the Court[43]. Since it is also true that referring a case on the basis of incompatibility with the fundamental freedoms requires a much bigger grasp of EC

37. See also on this issue, Paul Craig/Gráinne de Búrca, *EU Law...*,cit., pp- 493-494. Anthony Arnull, *The European Union....*, cit., pp. 104-114.
38. Paul Craig/Gráinne de Búrca, *EU Law...*, cit., p. 472; J. Komarek, "Federal Elements in the Community Judicial System: Building Coherence in the Community Legal System", *Common Market Law Review*, 2005, p. 9; Takis Tridimas, "The Court of Justice and Judicial Activism", *European Law Review*, 1996, pp. 204-207.
39. As Armin von Bogdandy argues: "Europaïsche Prinzipienlehre", *Europäisches Verfassungsrecht*, cit., p. 155 et seq.
40. See Advocate General Poiares Maduro, Opinion delivered on 7 April 2005 on Case C-255/02, *Halifax plc.*, points 62-72.
41. On Italy, Pasquale Pistone, "The Search for Objective Standards...", cit..., pp. 252-254.
42. Dirk Ehlers, "General Principles", *European Fundamental Rights and Freedoms*, (ed. by Dirk Ehlers), Berlin, 2007, p. 175.
43. On Interpretation and Vagueness in Law, Timothy A.O. Endicott, *Vagueness in Law*, Oxford, 2000, p. 57 et seq.

law (and a continuous keeping track of the ECJ case law), the inequalities affecting taxpayers are also much bigger in the latter case[44].

This example illustrates that had the ECJ never adopted the *acte clair doctrine*, we would not live in a EU with more references to the ECJ in direct tax issues, because the national courts would still have to decide whether the domestic tax provision raised any issues of interpretation of the EC Treaty fundamental freedoms[45].

Taking into account the current regime and contrary to the pessimistic view of Sarmiento[46], I am convinced that the advantages of the *CILFIT* doctrine largely overcome the disadvantages[47], and the system of precedent has been producing good results, in direct tax law issues as well. This assessment does not deny the need for reforming the judicial structure of the EU in the near future, but that is a different, even if complementary, issue [48].

2.3. CILFIT vs. Da Costa: the advantages of the system of precedent

Although the critics of the *CILFIT* doctrine normally do not criticize the *Da Costa* decision, it was in this ruling that the ECJ initiated what is very similar to a system of precedent: "The authority of an interpretation under Article 177 already given by the Court may deprive the obligation of its purpose and thus empty it of its substance. Such is the case especially when the question raised is materially identical with a question which has already been the subject of a preliminary ruling in a similar case"[49].

It results from *Da Costa* that a referral to the ECJ must raise a new fact or a new argument, because, otherwise, the ECJ will most probably reaffirm the

44. On the changing attitude of national tax courts, see. e.g. Axel Cordewener, "Personal Income Taxation of Non-Residents and the Increasing Impact of the EC Treaty Freedoms", *The Influence of European Law on Direct Taxation, Recent and Future Developments*, Ed. Dennis Weber, The Netherlands, 2007, pp. 35-40; "Germany", *Towards a Homogeneous...*, cit., pp. 140-146.
45. See Gerhard Bebr, "The Rambling Ghost of "Cohn-Bendit": *Acte Clair* and the Court of Justice", 20 *Common Market Law Review* 1985, p. 439 et seq.
46. "Who's Afraid...?", p. 72 et seq.;"Los 'Free-Lance' del Derecho Comunitario: La Desfiguración de la Doctrina CILFIT", *La Articulación entre el Derecho Comunitario y los Derechos Nacionales: Algunas Zonas de Fricción*, Madrid, 2006, p. 371 et seq.
47. Pasquale Pistone, on the contrary, supports the need to reformulate the CILFIT doctrine: "The Search for Objective Standards...", cit., p. 225.
48. See above footnote 8.
49. Paul Craig and Gráinne de Búrca, *EU Law...*, cit., p. 468.

doctrine of the previous case. In *CILFIT*, the Court seems to go a significant step further, because national courts of last instance may abstain from referring a case even if it is not "materially identical" to a previous one judged by the ECJ or "if there is no reasonable doubt as to the manner as the question raised is to be resolved" (see. 2.1. above).

However, for the purpose of the application of their doctrine by the national courts, the difference between *Da Costa* and *CILFIT*, like the aforementioned difference between para. 14 and para. 16 of *CILFIT*, is quantitative and not qualitative, and it is not very meaningful if we take into account that legal cases are seldom materially identical. Therefore, *Da Costa* already gave a broad discretion to last instance courts[50]. Also because the difference between *Da Costa* and paras. 14 and 16 of *CILFIT* is quantitative (it is also difficult to determine what a materially identical case is), *acte éclairé* and *acte clair* are interrelated concepts, as already argued above.

Besides, in *Da Costa*, one ruling is enough to create a precedent, whereas in *CILFIT*, the Court refers to "previous decisions" (and not to "settled case law"), in the English version, and to *giurisprudenza constante*, *gefestigte Rechtsprechung*, *jurisprudencia constante*. Even if "settled case law" is not necessary (the meaning of which is in turn difficult to determine), more than one decision seems necessary to eliminate any reasonable doubts on the existence of settled case law[51] (see however, *Meilicke*).

Another common point to the two cases is that both in *Da Costa* and *CILFIT*, national courts are encouraged to rely on prior rulings of the ECJ, whenever the substance of the legal issue has already been decided.

Such a system of precedent, as developed and reaffirmed by the Court in later cases, has several advantages: it has allowed the survival of the preliminary ruling mechanism as it was created in a Community of six Member States, in an increasingly enlarged European Union – although reforms will probably have to be initiated in the short term; it has a multiplier effect, as it creates a vertical relation between the ECJ and all the other courts, transforming it into a supreme court within the European Union, and transforming what seems to be a bilateral relation in a literal interpretation of the preliminary rulings, Art. 234, into a multilateral relation[52]. Thus, it broadens

50. See the *Cohn-Bendit* case and the others mentioned by Gerhard Bebr, "The Rambling Ghost of "Cohn-Bendit"..., cit., p. 440 et seq..
51. Gerhard Bebr, "The Rambling Ghost...", cit., p. 463.
52. See in respect of the multilateral relation, Paul Craig and Gráinne de Búrca, *EU Law...*, cit., pp. 474, 477.

the effect of an ECJ decision to all Member States. Even if some or many cases are wrongly not referred to the ECJ, the *Da Costa* and *CILFIT* doctrine, reaffirmed in *Köbler* and *Meilicke*, undoubtedly mean that all Member States are targets of the doctrine emerging from a decision.

The aforementioned ambiguity of the *acte clair* doctrine also allows the improvement of the ECJ jurisprudence, and in this perspective it is advantageous that there is no *stare decisis* rule (see also *Da Costa* and para. 15 of *CILFIT*). In *HAG GF*[53], the Court confronted the issue of overruling an earlier decision directly, saying that it had decided to reconsider its previous judgment (para. 10 et seq.). Advocate General Jacobs concluded in this case that "the Court has consistently recognised its power to depart from previous decisions... That the Court should in an appropriate case expressly overrule an earlier decision is I think an inescapable duty, even if the Court has never before expressly done so" (point 67)[54].

The flexibility resulting from the ambiguity of the *acte clair* doctrine has had some success in terms of relieving the ECJ of the increasing work overload, and of giving it significant freedom to evolve its case law, as well as giving some important space to national courts. However, it has not created much certainty for the targeted persons of the rules, namely for taxpayers, who depend on the interpretation of the *acte clair* doctrine by the national courts, and on the different chambers of the ECJ when a decision is referred to it.

Taking into account the ECJ case law on direct tax issues, it is still possible to a certain extent to determine what is settled case law (even if it can evolve if new facts or arguments appear), and what is not (and in this sense, what is clear and what is not), although I find it difficult to exactly follow a table like the one proposed by Pistone, aimed at reaching a secure level of settled case law[55]. For example contrary to what Pistone proposes in his table, according to the ECJ in *Meilicke*, domestic courts could have abstained from referring a case on inbound dividends since *Verkooijen*, the first ECJ decision on the issue. Besides, some discretion has to be left to national courts, and a good outcome will be assured, as long as national courts comply with Art. 10 EC Treaty, the general criteria of interpretation and the *CILFIT* criteria, and the ECJ pays more attention to the coherence of its decisions or expressly justifies changes in its case law, as it did in *HAG GF*.

53. ECJ 17 October 1990, Case C-10/89, *SA CNL-SUCAL NV v HAG GF AG.*
54. Delivered on 13 March 1990.
55. Pasquale Pistone, "The Search for Objective Standards...", cit., pp. 228-229.

Conclusions on settled case law on discriminatory and restrictive direct tax measures are addressed to the domestic legislator and the EC Council of Ministers, on one hand, and to the taxpayers, on the other hand. The first group of players must (should) be aware that a coherent and balanced direct tax regime requires a supranational effort of harmonization, whereas the taxpayers are protected by the multilateral effect of the ECJ case law. Whenever some issues on direct tax law are not yet clear, national courts, as part of the EC law vertical system, must refer the case to the ECJ, in order for a uniform interpretation and European integration to be achieved (Arts. 234(3), and 10 EC Treaty).

The following pages are devoted to discussing and identifying some of the clear and unclear issues.

3. The object and the development of the *Acte Clair* in Direct Tax Issues

3.1. Rules on the tax incidence, tax base, tax rates, anti-abuse and procedural rules

When we try to apply the *acte clair* doctrine to direct tax issues, we can begin by asking whether it is not already clear that the source and residence elements on which Member States' income tax law is based are to a certain extent incompatible with the fundamental freedoms of the EC Treaty[56].

This incompatibility resulting from discriminatory or restrictive tax measures based on the difference between residents and non-residents or taking into account the source state of income (home state vs. host state), can occur in respect of different kinds of tax rules:

- Rules on the tax incidence, including entitlement to a certain domestic tax regime by a certain category of taxpayers such as permanent establishments (see *Avoir Fiscal, Commerzbank, Futura, Royal Bank of Scotland, Saint-Gobain, XY, CLT-UFA, Deutsche Shell, Lidl Belgium*) or other non-residents (frontier workers) (*Schumacker, Wielockx, Asscher, Gilly, Geschwind, Zurstrasse, Wallentin, Conijn*) and definition of taxable person or group (*Zurstrassen, Metallgesellschaft*).
- Rules on the tax incidence and the tax base, such as the type of income and how to tax it in the case of a cross-border movement (tax on accrued but unrealized capital gains vs. tax on realized capital gains), deduction of business expenses, including insurance premiums, losses, maintenance payments, tax-free allowances and other personal or family-related costs, exemptions and methods for the valuation of assets and the calculation of the fiscal charge, (see most of the ECJ case law on direct taxation: *Bachmann, Danner, Skandia, Schilling, De Lasteyrie du Saillant, N, Safir, Bent Vestergaard, XAB/YAB, Gerritse, Scorpio, Centro Equestre da Lezíria Grande; Metallgesellschaft, Bosal, Weidert-Paulus, Keller Holding, Lankhorst-Hohorst, Thin Cap Group Litigation, Lammers & Van Cleeff, Fournier, Eurowings, ICI, Futura, Amid, Mertens, Marks & Spencer, Ritter-Coulais, Rewe Zentralfinanz, OyAA, Deutsche Shell, Lidl Belgium, Gilly, De Groot, Bouanich, Schempp, Jundt, Commission v. Portugal and Commission v. Sweden, Elisa, Commission v. France, Jäger*).
- Domestic exemptions or tax credits regarding double taxation, rates and tax progression (*Baars, Verkooijen, Lenz, Holböck, Maninnen, Meilicke, ACT Group Litigation, FII Group Litigation, Orange European Smallcap Fund, Royal Bank Scotland, CLT-UFA, Schumacker, Asscher, Biehl, Gilly, De Groot* and also *Commission v. France (Avoir Fiscal,) Saint-Gobain*), although it seems that Member States are free to choose the method for eliminating double taxation, even if it has restrictive effects (*Gilly, FII Group Litigation, Columbus Container*).
- Anti-abuse clauses and presumptions (*Cadbury Schweppes, Lankhorst-Hohorst, Thin Cap Group Litigation, Lammers & Van Cleeff, Lasertec, Talotta, Elisa* (indirectly) and *De Lasteryie du Saillant* (underlying very broad concept of presumption)): Nationals of Member States cannot attempt, under cover of the rights created by the Treaty, to improperly circumvent their national legislation (*Knoors*[57], *Bouchoucha*[58], *Centros*), but exercising a free movement in order to benefit from a more favourable regime is not sufficient to constitute abuse of that freedom (*Barbier, Centros, Halifax*[59], *Überseering, Inspire Art*[60], *Cadbury Schweppes, Thin Cap Group Litigation, Lammers & Van Cleeff*); however, a Member State can refuse granting a tax advantage if its system was designed to prevent conducts capable of jeopardizing the right of

56. See, e.g. Frans Vanistendael, "The ECJ at the Crossroads: Balancing Tax Sovereignty against the Imperatives of the Single Market", *European Taxation*, 2006, p. 413 et. seq.; Servaas van Thiel, "Why the ECJ Should Interpret Directly Applicable European Law as a Right to Intra-Community Most-Favoured-Nation Treatment", *The Influence of European Law on Direct Taxation*, cit., pp. 80-83.

57. ECJ, 7 February 1979, 115/78, *Knoors*.
58. ECJ, 3 October 1990, C-61/89, *Marc Gaston Bouchoucha*.
59. ECJ, 21 February 2006, C-255/02, *Halifax plc, and Others*.
60. ECJ, 30 September 2003, C-167/01, *Inspire Art Ltd*.

its taxing powers in relation to activities carried out in its territory (*Rewe Zentralfinanz*, para. 42 and *Oy AA*, para. 54).

- Administrative procedural rules, such as withholding taxes, tax declarations, deferral of taxation made subject to the provision of security, repayment of tax withheld at source, presumptions and exchange of information (*Biehl, Schumacker, Commerzbank, Futura, Bent Vestergaard, Gerritse, N., Scorpio, Centro Equestre da Lezíria Grande, Stauffer, Talotta, Elisa, A.*).

3.2. Definitions of taxpayer and tax object

It is, however, still disputable whether non-harmonized definitions of taxpayer and tax object come into the scope of the ECJ analysis, at least when they do not constitute illegitimate legal fictions with a restrictive effect in the internal market.

For example there are good arguments to consider that legal fictions like the one analysed in the *Van Hilten* case (according to which, nationals who, having resided in the Netherlands, die or make a gift within ten years after ceasing to reside there are deemed to have been resident in that state at the time of the death or of making the gift for the purposes of the inheritance tax) restrict free movement (among other consequences, it can lead to unjustified double taxation) and should therefore be considered incompatible with the fundamental freedoms.

The same reasoning could be applicable to too broad (possibly illegitimate) definitions of source, including a too broad definition of permanent establishment. Differences regarding definitions in Member States' (or Member States' and third countries') domestic legislation will often lead to double taxation (as in the *Van Hilten* case, should Switzerland have taxed the inheritance), and differences regarding definitions in bilateral tax treaties will lead to bilaterally more favourable treatments, although these are not incompatible with the Treaty, according to *D.* and *ACT Group Litigation.*

A parallel can be drawn with *De Lasteyrie du Saillant*, a case in which definition of tax object (meaning of capital gains for tax purposes) and tax base (when to tax capital gains) is strongly connected (a resident in France transferring his residence abroad was taxed on the increase in value determined in company securities at the moment of exiting the country, whereas a resident in France was only taxed on the realized capital gains). Somehow, there is an illegitimate definition of (unrealized) capital gains – the

ECJ decision in the *N.* case indirectly seems to confirm this interpretation of *De Lasteyrie du Saillant*, although the core of the issue in the latter was the underlying different tax treatment between (realized) capital gains belonging to residents and (non-realized) capital gains belonging to exiting residents.

It is true that, as a general rule, the EC "treaty offers no guarantee to a citizen of the Union that transferring his activities to a Member State other than that in which he previously resided will be neutral as regards taxation" (*Schempp*, para. 45; see also *Deutsche Shell*, paras. 42 and 43), but Member States must nevertheless exercise their retained powers in compliance with Community law (*Schumacker*, para. 21, *ICI*, para. 19, *X and Y*, para. 32, *De Lasteyrie du Saillant* , para. 44, *Marks & Spencer*, para. 29, *N.*, para. 33 and so on).

Applying these statements to definitions of taxpayers and income, I would say that for the purposes of their analysis under the fundamental freedoms, definitions belong to the allocation of taxing rights rules, and are under the competence of the Member States, as long as they do not lead to restrictions incompatible with the fundamental freedoms, but the position of the ECJ on these issues does not yet constitute settled case law.

3.3. Tax treaty rules

According to settled case law, the first step in order to verify whether the direct tax rules based on the distinction between residents and non-residents are discriminatory or restrictive is to acknowledge whether the situation of residents and non-resident taxpayers is comparable. That comparison regards, in the first place, domestic tax legislation and, in the second place, bilateral tax treaties. The relevance of the regime in a tax treaty in order to reach a final decision on discrimination and or restriction of fundamental freedoms still needs further development of case law.

Some issues can be considered clear: For example "in the absence of unifying or harmonizing Community measures, Member States retain the power to define, by treaty or unilaterally, the criteria for allocating their powers of taxation, particularly with a view to eliminating double taxation" (*Gilly*, paras. 24 and 30; *Saint-Gobain*, para. 57; *De Groot*, para. 93, *Van Hilten*, para. 47; *N.*, para. 43, *ACT Group Litigation*, para. 52).

Also, Member States may find inspiration in international practice, particularly in the OECD Model Tax Convention, namely regarding connecting factors for the purpose of allocating tax jurisdiction, and solutions that prevent avoidance and evasion (*Gilly*, para. 31 (paras. 23 et seq.), *Van Hilten*, para. 48; *N.*, paras. 45 and 46).

But it is not clear to what extent allocation-of-taxing-rights rules in double taxation conventions are outside the scope of the ECJ (in *Deutsche Shell*, an allocation-of-taxing-rights rule was accepted, but the domestic rule on deduction of foreign currency losses was considered to be incompatible with the Treaty, paras. 41-45), e.g. whether they can introduce a discriminatory cash-flow disadvantage (cf. *FII Group Litigation* and *Metallgesellschaft*) and whether any rule within a treaty is to be considered an allocation-of-taxing-rights rule. *D.* and *ACT Group Litigation* indicate that the ECJ did not want to distinguish between categories of rules within a tax treaty (allocation of taxing rights, anti-abuse clause, tax benefits clause), but taking into account the lack of arguments put forward by the Court in the aforementioned cases, it is premature to consider that it is settled case law[61].

It is not clear either, whether and to what extent rules in double taxation conventions compensate discriminatory/restrictive treatment of domestic tax laws: although in *Commerzbank*, the Court followed its Advocate General's Opinion and noted that non-resident companies were placed at a disadvantage by the refusal of the repayment supplement (para. 18), which could not be justified by the exemption of the US-source income from tax as a result of the tax treaty, the role of the tax treaties in allocating tax jurisdiction and thus achieving a fair distribution of revenue between the contracting states and compensating any domestic restrictive treatment has not been clarified yet (*Marks & Spencer*, *ACT Group Litigation*, *FII Group Litigation*, *Denkavit Internationaal*, *Amurta*).

In *Bachmann*, as Van Thiel explains in his paper, the Court gave priority to the revenue interests of a single Member State and disregarded the market integration required by the EC Treaty, by accepting that Member States take discriminatory measures to safeguard the coherence of their tax systems if they fail to reach agreement on an alternative solution by means of tax treaties or harmonization. In *Wielockx*, however, the ECJ considered that tax treaty rules are relevant to ensure compliance with Community law through coherence at a macro level by the reciprocity of a bilateral tax treaty, and in this way the Court reinforced its doctrine in *Commission v. France* [62].

61. See, on the issue, Axel Cordewener/Ekkehart Reimer, "The Future of Most-Favoured-Nation Treatment in EC Tax Law – Did the ECJ Pull the Emergency Brake without Real Need?– Part 2", *European Taxation*, 2006, pp. 294 et seq.; cf. Vogel/Gutmann/Dourado, "Tax Treaties between Member States and Third States: 'Reciprocity' in Bilateral Tax Treaties and Non-discrimination in EC Law", *EC Tax Review*, 2006, pp. 83 et seq.

Wielockx seems to go in the right direction, but in order to be consistent, this doctrine has to be combined with the issue on allocation-of-taxing-rights rules in tax treaties. If, taking into account the characteristics of a bilateral tax treaty, allocation-of-taxing-rights rules cannot be extended to taxpayers who are outside its scope, as the Court well clarified in *D.* and in *ACT Group Litigation*, tax treaty rules introducing a discriminatory disadvantage to its addressees should be considered incompatible with the fundamental freedoms, and the situation solved as required by Art. 307 EC Treaty. It is more difficult to argue that tax treaty rules, such as tax sparing credits, considered to be harmful by the OECD, should be distinguished from the allocation-of-taxing-rights rules and subject to a non-discrimination assessment, as long as those rules are not considered to be harmful tax regimes by the EU competent *ad hoc* groups or institutions[63].

3.4. Unclearness around double taxation relief rules

Whereas it would seem clear that double taxation relief rules in tax treaties cannot be discriminatory/restrictive, because the fundamental rights conferred by the EC Treaty "are unconditional and a Member State cannot make respect for them subject to the contents of an agreement concluded with another Member State" (see, in respect of the right of establishment involving permanent establishments, para. 26, *Avoir Fiscal*; *Royal Bank of Scotland*, para. 31 *X AB/Y AB*; *Saint-Gobain*), the ECJ decision in *FII Group Litigation* goes in a different and unclear direction, as it confers on a Member State the right to exempt domestic dividends according to domestic law, and apply an imputation credit to inbound dividends according to a tax treaty, creating a cash-flow disadvantage in respect of the latter. The *Columbus Container* decision, where the compatibility of the German Foreign Transaction Tax Law switch-over mechanism on double taxation relief of a foreign PE (this German legislation has the same objectives as CFC rules) with the fundamental freedoms was analysed, is also difficult to explain: although partnerships such as Columbus do not suffer any tax disadvantage

62. Cf. Servaas van Thiel, "Justifications in Community Law for Income Tax Restrictions on Free Movement: acte clair rules that can be readily applied by national courts", in this book, p. 90.
63. Vogel/Gutmann/Dourado, "Tax Treaties…", cit., pp. 83 et seq.

in comparison with partnerships established in Germany, and therefore, no discrimination results from a difference in treatment between those two categories of partnerships, the switch-over in tax relief rules differentiates among the host Member States of the German outbound investment, rendering less attractive the exercise of the freedom of establishment in respect of the Member States to which the switch-over mechanism is applicable. In other words, the difference in treatment creates a tax disadvantage for the resident company to which the switch-over mechanism is applicable and should accordingly be regarded as constituting a restriction taking into account the same reasoning of *Cadbury Schweppes* even if at the next step of analysis a relevant justification were acceptable[64].

3.5. The comparison tests

Another unclear issue concerns the relevance of the host state tax treatment to the home state's complying with the fundamental freedoms, both in respect of unilateral domestic rules and bilateral tax treaty rules (cf. *Manninen, Meilicke, ACT Group Litigation, FII Group Litigation, N., Schempp*). This is a field where the case law still has a long path to go. An example of this is the comparison test. Originally, the test was used to compare whether residents and non-residents are in the same objective situation for tax purposes, but it has recently been extended by the Court, in order to achieve the "legitimate objective of allocating the power of taxation, in particular for the purposes of eliminating double taxation between Member States" (*N.*, para. 49).

3.5.1. The comparison between residents and non-residents

Under the perspective of the taxpayer referring a case to the Court and therefore taking into account the structure of the ECJ case law under Art. 234 EC Treaty, the aforementioned examples of discriminatory/restrictive tax rules can be organized under two main headings: one concerning the prohibition of discriminatory/restrictive exit taxes by the home Member State on outbound movements, and the other regarding discriminatory/restrictive access taxes by the host Member State on inbound movements[65]. Together, these prohibitions ensure a non-restrictive tax regime within the internal market.

64. See also ECJ, 30 November 1995, Case C-55/94 *Gebhard*, para. 37; ECJ, 5 October 2004, Case C-442/02 *Caixa Bank France*, para. 11; *Cadbury Schweppes*, para. 45.
65. See, e.g. Servaas van Thiel, "Why the ECJ...", cit., pp. 80-83.

The Court uses an equivalent formula, concerning all fundamental freedoms, in order to hold that restrictions to non-residents from investing in the host state as well as to residents who are deterred from raising capital from non-resident investors are incompatible with the EC Treaty: for example in the *Daily Mail*, *ICI* and *X/AB* and *Y/AB* cases, all of them regarding the freedom of establishment, the Court stated as follows: "As far as the provisions concerning freedom of establishment are concerned, it must be pointed out that, even though, according to their wording those provisions are mainly aimed at ensuring that foreign nationals and companies are treated in the host Member State in the same way as nationals of that State, they also prohibit the Member State of origin from hindering the establishment in another Member State of one of its nationals or of a company incorporated under its legislation which comes within the definition contained in Article 58 [currently Art. 43] of the Treaty" (see *Daily Mail*, para. 16; *ICI*, para. 21, *X/AB and Y/AB* , para. 26; and cf. para. 36 of *X and Y case*: "The refusal of the tax advantage in question on the ground that the transferee company in which the taxpayer has a holding is established in another Member State, is likely to have a deterrent effect on the exercise by that taxpayer of the right conferred on him by Article 43 to pursue his activities in that other Member State through the intermediary of a company").

In *Safir* (para. 23), the ECJ held that "in the perspective of a single market and in order to enable its objectives to be attained, Article 59 of the Treaty likewise precludes the application of any national legislation which has the effect of making the provision of services between Member States more difficult than the provision of services exclusively within one Member State" (cf. *Commission v. France*[66], para. 17).

And in *Bouanich*, in which compatibility of domestic tax legislation with the free movement of capital was being analysed, the ECJ, in para. 34, citing the Advocate General's Opinion (paras. 33 and 34) considered that "the effect of such legislation is to make cross-frontier transfer of capital less attractive both by deterring investors who are not resident in Sweden from buying shares in companies resident in Sweden, and also, consequently, by restricting the opportunities available to Swedish companies to raise capital from investors who are not residents in Sweden".

Taking into account the aforementioned case law, I reach the general conclusion that the tax provisions in the income tax codes and tax treaties, creating a domestic and bilateral regime based on the source and residence

66. ECJ, 5 October 1994, Case C-381/93.

classification (worldwide of net income taxation aimed at taxing the ability-to-pay vs. source taxation of gross income at flat rates), distinguish taxpayers who in many cases are in the *same position* under the fundamental freedoms – including capital movements and payments –, independently of their place of residence and the place where the capital is invested. Although, according to Art. 58(1)(a) EC Treaty, it is possible to tax residents and non-residents who are not in the *same position* differently (which seems to be a rule, according to the drafting technique), unless there is an arbitrary discrimination (which seems to be an exception, according to the drafting technique), it results from settled case law, that Art. 58(1)(a) EC Treaty, is, after all, an exception, whereas most domestic income tax rules involving an assessment on free movement of capital and payments are covered under Art. 58(3) EC Treaty (*Verkooijen*, para. 43, *Lenz*, paras. 27, 32, *X & Y*, paras 49, 72, *Barbier*, para. 73, *Manninen*, para. 19, *Meilicke*, para. 19, *A.*, para. 19, *Elisa*, paras. 86-92, *Orange*, paras. 85, 97, 107-108).

3.5.2. Recent comparison tests

The test now covers the aforementioned comparison between resident and non-resident taxpayers (*Denkavit Internationaal*, para. 35); the comparison between the tax advantage granted in favour of a shareholder and the tax payable by way of corporation tax - the cohesion of the tax system is assured as long as that correlation exists (*Maninnen*, para. 46; *Meilicke*, para. 29); the comparison between the host and the home states (*N.*, paras. 49, 54, 55, *ACT Group Litigation*, paras. 58-60); and the comparison of the tax situation of the recipient of the taxpayer's deductible amounts (*Schempp*, para. 35).

The Court has held that the comparison test between a home and a host state also means that the allocation of taxing rights rules in a tax treaty implies that a home Member State cannot be required to take account, for the purposes of implementing a tax treaty and applying its tax law, of the tax treatment given in the host state, solely because negative results in the host state are not taken into account for tax purposes (*Deutsche Shell*, para. 42; cf. *Schempp*).

On the other hand, the home Member State must take into account the tax treatment given in the host state, in the case of discriminatory economic double taxation (*Maninnen* and *Meilicke*), and, for example in the case of a regime of deferred payment of a capital gains tax, due upon the transfer of residence by a taxpayer, and conditional on the provision of guarantees,

where there are reductions in value arising after the transfer of residence by the person concerned and they are not taken into account by the host state (*N.*, paras. 54-55).

It seemed to be settled case law that any advantage resulting from the low taxation in which a subsidiary benefits in its home (and host) Member State cannot be offset by less favourable treatment of the parent company established in another Member State (*Commission v. France*, para. 21, *ICI*, para. 29, *Eurowings*, para. 44, *Skandia*, para. 52, *Cadbury Schweppes*, para. 49). The same applies to the other fundamental freedoms where the host state has a lower taxation than the home state and the latter argues that its regime aims at offsetting that advantage (*Svensson and Gustavsson*, para. 18; *Asscher*, para. 58; *Bent Vestergaard*, para. 24, *X and Y*, para. 52, *Staufer*, para. 53). However, *Columbus Container* goes in the opposite direction allowing such compensation in the case of low taxation benefiting a permanent establishment in the host Member State: According to the ECJ, "[b]y applying the set-off method to such foreign partnerships, that legislation merely subjects, in Germany, the profits made by such partnerships to the same tax rate as profits made by partnerships established in Germany" (para. 39). "Since partnerships such as Columbus do not suffer any tax disadvantage in comparison with partnerships established in Germany, there is no discrimination resulting from a difference in treatment between those two categories of partnerships" (para. 40).

3.6. Negative limits: the borderline of the tax *acte clair*

Some of the limits accepted by the ECJ to discriminatory and restrictive tax rules (negative limits) can also be considered *acte clair*.

The assertion, according to which, resident and non-resident taxpayers who are not in a comparable position can be differently treated (i.e. different tax treatment will neither be considered discriminatory nor restrictive) is uncontroversial (although it is not uncontroversial what a comparable position is) and one of the frontiers of the analysis on discriminatory tax provisions – see *Schumacker, Gilly, Verkooijen, Maninnen, Blanckaert, Bouanich, Deutsche Shell.*

Besides, the fact that the ECJ accepts justifications to tax discrimination and restrictions, which are not expressly mentioned in the Treaty, is another negative limit to the decision of incompatibility of domestic and tax treaties

rules in respect of the EC Treaty – the contours of which I will analyse in point 4 and have been the topic of Van Thiel's paper[67].

Furthermore, the caution the ECJ has taken in recent cases regarding bilateral tax treaties (avoiding declaration of a most-favoured nation (MFN) clause and of incompatibility of limitation-on-benefits (LOB) clauses) shows that the ECJ is not (yet) prepared to ultimately enlarge the scope of the prohibition to comparison among non-residents (although in *Cadbury Schweppes* that comparison was made and in *Columbus Container* suggested by the Advocate General[68], but ignored by the Court).

Because under Art. 234 EC Treaty, the ECJ has been asked to interpret the compatibility of different types of very concrete tax rules and tax regimes with the fundamental freedoms, the Court has to adopt a step-by-step approach. The methodology is not different from the one followed in respect of other types of rules – see the example of anti-abuse rules[69] - but being applied to tax law rules, it means that the whole structure of the tax codes based on the duality residents/non-residents is progressively disappearing.

3.7. Principles

The ECJ case law has not only regarded the aforementioned types of tax rules but has also contributed to (re)defining the tax law principles in the EU.

Domestic tax law principles recognized by international tax law such as the ability-to-pay, net income taxation and progressive taxation, traditionally linked to taxation of residents, as well as the burden of proof connected to the so-called cooperation duties of the taxpayer within the tax relationship and the principle of practicability, interpreted in the light of the fundamental freedoms, are acquiring a new shape within the EU.

67. Servaas van Thiel, "Justifications in Community Law…", cit., p. 85 et seq.
68. Advocate General Mengozzi, Opinion on *Columbus Container.*
69. See Rita de La Feria, "Prohibition of Abuse of (Community) Law – The Creation of a New General Principle of EC Law Through Tax?", Oxford University Centre for Business Taxation, *WP 07/23*).

3.7.1. The ability-to-pay principle

Concerning the ability-to-pay principle, on the one hand, the ECJ recognizes that the ability to pay tax, determined by reference to the taxpayer's aggregate income and his personal and family circumstances, is easier to assess at the place where his personal and financial interests are centred and that this will normally be the place where he has his personal abode (*Schumacker*, paras. 31-32; *Geschwind*, para. 22; *Zurstrassen*, para. 21; *De Groot*, para. 98; *Gerritse*, para. 43; *Wallentin*, para. 15; *Meindl*, para. 23). As a rule, cross-border individual income and expenses cannot be subject to less favourable tax treatment (see *Jundt*). In *De Groot*, the maintenance obligations and the tax-free allowances as a result of the taxpayer's personal and family circumstances were to be taken into account by the residence state, in full and not according to a proportionality factor (in proportion to the income derived in the home state) – otherwise the rule discriminated/restricted outbound activities.

In this context, the tax credit granted for reduction/elimination of economic double taxation to a shareholder who is fully taxable in a Member State for income tax purposes is to be calculated in a way that a correlation between the tax credit granted in favour of the shareholder and the tax payable by way of corporation tax is maintained, even if the shares are held in a company established in another Member State (*Maninnen*, para. 46, *Meilicke*, para. 29).

The state of residence (the home state) may be released from the aforementioned obligations if it finds that, in the absence of a convention, one or more states of employment grant advantages based on the personal and family circumstances of non-resident taxpayers, regarding the taxable income received in those host states (*De Groot*, para. 100).

In contrast, the state of employment (the host state) is required to take into account personal and family circumstances only where the taxpayer derives almost all or all of his taxable income from employment in that state and where he has no significant income in his state of residence, so that the latter is not in a position to grant tax allowances relating to those circumstances (*Schumacker*, para. 36, *Gschwind*, para. 27, *De Groot*, para. 89; *Gerritse*, para. 48; *Wallentin*, paras. 17-19; *Lakebrink*, para. 36)[70].

70. See on the ability-to-pay principle, Pasquale Pistone, "The Search for Objective Standards…", cit., pp. 255-257.

However, in *Schempp*, the Court decided that non-deductibility of payment of maintenance amounts in the home state of the payer, in case the recipient resides in a different Member State and in which state the maintenance is not taxable, is not precluded by Arts. 12 and 18(1) EC Treaty. According to the ECJ, the payment of maintenance to a recipient resident in the home state of the payer and to a recipient resident in another Member State are not comparable, because the recipients are subject to different tax systems (para. 35 et seq.). Instead of analysing the tax treatment given to resident taxpayers according to whether they are paying the maintenance to a resident or a non-resident (as has been done in respect of the secondary right of establishment, *Saint-Gobain*, *Marks & Spencer*, *Bosal*, *Keller Holding*, *Rewe Zentralfinanz*), it is the tax treatment of the recipient of the income in the different Member States that is being compared.

This is not the *Bachmann* argument of cohesion, according to which there must be a direct link between the tax advantage concerned and the offsetting of that advantage (i.e. a direct link regarding the same taxpayer liable to income tax, between the possibility of deduction and subsequent taxation of the sums (*Svensson and Gustavsson*, para. 18, *Asscher* para. 58, *ICI*, para. 29, *Bent Vestergaard*, para. 24, *X and Y*, para. 52, *Maninnen*, para. 42)) but the meaning given to cohesion in *Wielockx*: the ECJ shifts the argument of cohesion to the reciprocity of the rules applicable in the Member States involved (see also *Wielockx*, paras. 23-27).

But this means, that, as in a domestic tax system, deduction of maintenance expenses is a right not strictly connected with the ability-to-pay of a resident taxpayer, but subject to taxation of income of the recipient. It is neither related to the taxpayer's residence or to the state where he exercises his activities, but with the location of the recipient of the income and subject to the tax treatment given to the latter. As a consequence, it is likely that deduction of maintenance expenses will neither be taken into account by the state where he/she resides nor by the state where the recipient of the amounts resides.

3.7.2. The net income taxation principle

The net income taxation principle, traditionally connected with taxation of resident taxpayers and permanent establishments regarding the activity exercised within the territory of residence/of the permanent establishment's location, and with a "rule of symmetry", is also rejected by settled case law and is being reshaped – see *Bent Vestergaard, XAB/YAB, Gerritse, Scorpio,*

Centro Equestre da Lezíria Grande, Bosal, Weidert-Paulus, Keller Holding, Lankhorst-Hohorst, Fournier, Eurowings, ICI, Futura, Amid, Mertens, Marks & Spencer, Ritter-Coulais, Rewe Zentralfinanz, Oy AA, Lidl Belgium, Deutsche Shell.

First, net income taxation is also enlarged to non-residents, regarding business expenses (*Gerritse, Scorpio* and *Centro Equestre da Lezíria Grande*). However, comparison between residents and non-residents requires some caution: withholding taxes on non-residents are not precluded by the Treaty and are even necessary in order to ensure taxation at source (*Scorpio*); and whereas expenses directly linked to the activity may be deducted in the withholding procedure (*Scorpio*, para. 50, *Centro Equestre da Lezíria Grande*, para. 24-25, 27), other business expenses can be taken into account in a subsequent refund procedure (*Scorpio*, paras. 50-52, *Centro Equestre da Lezíria Grande*, para. 24)[71].

Second, in the context of (non-) deduction of costs and losses incurred outside the territory of the Member State of residence, or involving a resident in another Member State (deduction of interest paid to a non-resident, for example), the principle of territoriality used to serve as landmark for an effective fiscal supervision and was adequate to broadly preventing avoidance and tax planning schemes, such as the transfer of loss-making activities to states (including Member States) with lower taxation than the residence state (see the arguments of the German government in *Rewe Zentralfinanz*, paras. 38-50 and the counter argument of Advocate General Poiares Maduro, at point 52[72]).

In this respect, the ECJ seems to only accept the argument of balanced allocation of taxing powers "in conjunction with two other grounds, based on the taking into account of tax losses twice and on tax avoidance" (Opinion of Advocate General Poiares Maduro, *Rewe Zentralfinanz*, points 26-28, *Rewe Zentralfinanz*, para. 41, *OY AA*, paras. 51-56) and not as a "rule of symmetry" between the right to tax a company's profit and the duty to take that company's losses into account (*Rewe Zentralfinanz*, paras. 27, 53, *Bosal*, para. 37-40, *OY AA*, para. 43).

71. See Pasquale Pistone, "Kirchberg 3 October 2006: Three Decisions that Did...Not Change the Future of European Taxation", *Intertax*, 2006, p. 584.
72. Opinion delivered on 29 March 2007, Case C-347/04.

3.7.3. The prohibition of abuse of law

Furthermore, the requirement that anti-avoidance rules/regimes are only allowed when a purely artificial arrangement exists (*Cadbury Schweppes*; cf. *Centros, Halifax*), is much more restrictive to Member States than many of the (still) existing anti-abuse clauses as well as non-rebuttable presumptions in domestic tax legislation. It seems that this reasoning is not applicable to some personal/family expenses where the reciprocity of the rules applicable in the Member States involved is to be considered (cf. the above in respect of *Schempp* and ability-to-pay). It can also be asked whether the argument of safeguarding the balanced allocation of taxing powers combined with the risk of tax avoidance by means of purely artificial arrangements, as was used in *Oy AA* (paras. 58-62), does not go (much) beyond *Cadbury Schweppes*. Taking into account the concrete legislation, it does not. If the Finnish tax regime for deductibility of an intra-group financial transfer, gave the companies the right to elect any Member State to deduct their losses, it would jeopardize the right of the Member State to exercise its taxing powers in relation to activities carried out in its territory (*Rewe Zentralfinanz*, para. 42; *Oy AA*, para. 45): what becomes unclear is whether the right to deduct losses within the EC (in the home Member State of any company belonging to the group) by a company resident in a different Member State is limited to liquidation losses, as Pistone argues in his paper[73].

3.7.4. The principle of territoriality

It follows from the preceding paragraphs that the principle of territoriality is itself being reshaped. This is happening in respect of different situations: taxation of gross income versus taxation of net income; correlation between the sums that are deducted or exempted from the taxable income and the sums which are subject to tax within the same Member State – see *Wielockx, Safir, Lankhorst-Hohorst, Thin Cap Group Litigation*, as well as the cases involving discrimination of permanent establishments, such as *Commission v. France, Saint-Gobain, Deutsche Shell*; tax credits granted to shareholders fully taxable in a Member State, according to the place of establishment of the companies in which the shares are held (*Maninnen*, para. 46 and *Meilicke*, para. 29); effective fiscal supervision called upon by

73. "The Search for Objective Standards..." cit., point 2.3.1., pp. 237-240, and whether cash-flow disadvantages are going to play any role in assessing that right, as the Advocate General Sharpston argues in his Opinion in Lidl Belgium (Opinion of Advocate General Sharpston delivered on 14 February 2008, Case C-414/06 Lidl Belgium GmbH & Co. KG v Finanzamt Heilbronn, points 25-30).

the Member States; the principles of practicability and simplicity through presumptions, which were thought of in the context of the activity of the tax administration within the territory of the Member State (*Cadbury Schweppes*, *Lankhorst-Hohorst, Tallota*, indirectly, *Elisa*) as they are normally considered to be disproportionate to the followed aim.

3.8. The object of the *acte clair* doctrine in direct tax issues involving Member States and third states

The main question raised above (3.1.) concerned the issue of whether the ECJ case law on discriminatory and restrictive tax measures is not already settled in respect of the incompatibility, to a certain extent, of the source and residence elements on which Member States' income tax law is based, with the EC Treaty.

If I now consider the free movement of capital involving Member States and a third state (which is not a Member of the EU, EEA or EFTA), under Arts. 56 to 58 of the Treaty, some issues have to be approached differently.

It is not yet clear, in tax matters, whether nationals of third states are entitled to the free movement of capital or whether this only applies to nationals of a Member State investing in a third state[74], and there are good arguments not to automatically enlarge the tax rules applicable to EU nationals to non-EU nationals[75]. However, some arguments go in the direction of recognizing protection to third states' nationals in direct tax issues as well: In the *A.* case, the Court clarifies that capital movements between Member States

74. See on this discussion, Pasquale Pistone, "General Report", *The EU and Third Countries: Direct Taxation, Michael Lang/Pasquale Pistone (Hrs.),Wien, 2007, p. 15 et seq.*; Ana Paula Dourado, "National Report Portugal", *The EU and Third Countries...*, cit., p. 501 et seq.; Daniel S. Smit, "The Relationship between the Free Movement of Capital and other EC Treaty Freedoms in Third Country Relationships in the Field of Direct Taxation: a question of exclusivity, parallelism or causality?", *EC Tax Review*, 2007, p. 252 et seq.; Axel Cordewener/Georg W. Kofler/Clement Philipp Schindler, "Free Movement of Capital, Third Country Relationship and National Tax Law: An emerging issue before the ECJ", *European Taxation,* 2007, p. 107 et seq.; "Free Movement of Capital and Third Countries: Exploring the outer boundaries with *Lasertec*, *A and B* and *Holböck*", *European Taxation* , 2007, p. 371 et seq.

75. Ana Paula Dourado, "National Report Portugal", *The EU and Third Countries...*, cit., pp. 501-518; Wolfgang Schön, "Der Kapitalverkehr mit Drittstaaten und das Internationale Steuerrecht", in Gocke/Gosch/Lang(eds.), *Körperschaftssteuer, Internationales Steuerrecht, Doppelbesteuerung, FS für Franz Wassermeyer zum 65. Geburtstag,* 2005, p. 489 et seq.; Kristina Stahl, "Free Movement of Capital between Member States and Third Countries", *EC Tax Review,* 2004, p. 47 et seq.

and third states may be relied before national courts (para. 37); this is confirmed in the *Orange* case (cf. paras 87-88, 95-97); in non-tax matters it seems to be uncontroversial that third states' nationals are covered by the freedom of capital (see the *Kadi* and *Al Barakaat* cases[76]). Also, according to Art. 60 EC Treaty, regarding interruption of economic relations with one or more third states, the Council may take the necessary urgent measures on the movement of capital and payments as regards the third states concerned, and this includes movement of capital with the nationals of those states.

But some issues of general nature can be considered clear, as deriving directly or indirectly from settled case law. A group of those issues relate to overlapping of freedoms, in the case where any (other) fundamental freedom prevails over the free movement of capital (the ECJ has recently reaffirmed that in the case of overlap of freedoms, the purpose of the tax legislation is decisive in order to decide which is the relevant freedom: *FII Group Litigation, Holböck*):

A permanent establishment of a third state is not entitled to a Member State's domestic tax regime as it is governed by the freedom of establishment rules and not by the free movement of capital rules (see *Avoir Fiscal, Commerzbank, Futura, Royal Bank of Scotland, Saint-Gobain, XY, CLT UFA, Deutsche Shell, Lidl Belgium*).

The same applies to inbound investments (an investment in the EU from a third-state national), to non-resident workers (and frontier workers) nationals of a third state, and to services provided by a third-state national (cf. *Fidium Finanz*), as long as they are covered by the freedom of establishment, the free movement of workers or the free movement of services, respectively.

Another group regards the argument of effectiveness of fiscal supervision, which is being interpreted much more broadly, taking into account that Directive 77/799/EEC is not applicable between Member States and third states (*Van Hilten, FII Group Litigation, A.*).

76. See, on the Regulation by the Council to implement the order to freeze funds and financial resources in the Community, belonging to a third state national, Opinion of Advocate General Poiares Maduro, delivered on 16 January 2008, C-401/05 P, *Kadi,* point 11 et seq.: it is not even disputed that, unless an exception is applicable, the free movement of capital involves third countries nationals (cf., Opinion of Avocate General Poiares Maduro, delivered on 23 January 2008, C-415/05 P, *Al Barakaat,* points 2-16).

3.9. The adequate level of abstraction: the example of the tax base

If we take the example of the tax base elements, we can find settled case law in respect of different levels of abstraction. Among several possibilities, we may choose the treatment of inbound dividends, since this aspect was expressly considered in *Melicke* to have been settled case law from *Verkooijen* on (cf. point 6 below and *Manninen, Kerkhaert-Morres, FII Group Litigation, Meilicke; Verkooijen, Lenz, Holböck*). It seems clear, as Pistone argues[77], that systems that integrate profits and dividends are to be extended to inbound dividends, and in the case of classical and schedular systems the same tax rate is to be applicable to inbound dividends; moreover, still following Pistone, whereas in the case of Member States adopting the credit method, the ECJ uses a pan-European approach regarding inbound dividends, in the case of outbound dividends, the Court follows a per-country approach[78].

Settled case law also exists to some extent in respect of the treatment of losses: the Court accepted the territoriality principle, according to which the Member State is obliged to offset the losses linked to the economic activity of the company in the home State (*Futura, Marks & Spencer, Rewe Zentralfinanz, Deutsche Shell*), unless losses of a subsidiary cannot be compensated in its home State (*Marks & Spencer*). However, the applicability of *Marks & Spencer* to other EU regimes, for example to the Swedish or Finnish contribution systems, or to the Netherlands full fiscal consolidation regime was not clear (cf. *Oy AA*) [79].

Another example of settled case law concerns the prohibition of non-rebuttable presumptions or other national measures restricting freedom of establishment targeted at preventing tax avoidance/tax evasion: such a national measure may be justified where it specifically targets wholly artificial arrangements designed to circumvent the domestic legislation concerned (*ICI*, para. 26; *Lankhorst-Hohorst*, para. 37; *Marks & Spencer*, para. 57; *Cadbury Schweppes*, paras. 51, 55, *Thin Cap Group Litigation*, paras. 72, 74,

77. Pasquale Pistone, "The Search for Objective Standards...", cit., p. 241.
78. Pasquale Pistone, Id., cit., p. 244; See also, Frans Vanistendael, "*Denkavit Internationaal:* the balance between fiscal sovereignty and the fundamental freedoms", *European Taxation,* 2007, p. 210 et seq.
79. See Pasquale Pistone, Ibid., pp. 237-240; Michael Lang, "The Marks and Spencer Case – The Open Issues Following the ECJ's Final Word", *European Taxation,* 2006, p. 54 et seq.; Sjoerd Douma/Caroline Naumburg, "Marks & Spencer: Are National Tax Systems Éclairé?", *European Taxation,* 2006, p. 431 et seq.

Lammers & Van Cleeff, para. 28, *Talotta*, para. 25, *Elisa*, para. 98) and respects the principle of proportionality (*Thin Cap Group Litigation*, para. 82, *Lammers & Van Cleeff*, para. 32, *Oy AA*, para. 63). Within this group of non-rebuttable presumptions, at a more concrete level, certain aspects regarding discriminatory thin capitalization rules are also clear (at least, that this is a regime to be analysed under the freedom of establishment (*Lankhorst-Hohorst, Thin Cap Group Litigation, Lasertec, Lammers & Van Cleeff*).

The most difficult question concerning this type of analysis – which specific aspects of the case law (in direct tax issues) are clear and which are not – is whether it is possible to determine the extent to which the source and residence elements on which Member States' income tax law is based are incompatible with the fundamental freedoms of the EC Treaty.

If the Court decided that the fundamental freedoms required the applicability of two other principles of intermediate level in direct tax issues – the principle of national treatment and of a most-favoured-nation clause[80] – the results of the case law would be much easier to predict (although not necessarily better for the taxpayer) and the case law itself would be much simpler. Otherwise, the ECJ case law will have to endlessly analyse the non-harmonized tax regimes[81]. The disadvantage of the latter methodology lies essentially in the fact that case law on detailed aspects of the tax regimes will not necessarily bring more certainty, but the taxpayer may have no other choice than to try to have a referral made by a domestic court (or that it decides that the national legislation is incompatible with the fundamental freedoms).

But it is not clear either that the fundamental freedoms would require the applicability of the principles of national treatment and of a most-favoured-

80. Cf., among many others, Servaas van Thiel, "Why the ECJ...", cit., pp. 91 et seq.; Georg Kofler, "Most Favoured Nation Treatment in Direct Taxation: Does the EC law provide for Community MFN in bilateral double taxation treaties?"*Houston Business and Tax Journal*, 2005, p. 4 et seq. and the literature references therein; Axel Cordewener/Ekkehart Reimer, "The Future of Most-Favoured-Nation Treatment...", cit., p. 291 et seq.; Weber/Spierts, "The 'D' case: Most-Favoured-Nation Treatment and Compensation of Legal Costs before the Court of Justice", *European Taxation*, 2004, p. 65 et seq.; Ines Hofbauer, "DBA Diskriminierungsverbote und gemeinschaftsrechtliche Grundfreiheiten – Meistbegünstigung", *Diskriminierunbgsverbote im Recht der DBA*, (Hrs. Lang, Schuch, Staringer), Wien, 2006, p. 299 et seq.

81. Cf. as an example Paul Farmer, "Striking a Proper Balance between the National Fiscal Interest and the Community Interest – a Perpetual Struggle?", *The Influence of European Law on Direct Taxation*, cit., pp. 31-34.

nation clause to direct tax law[82]. The comparability tests used by the Court, probably aimed at constructing a cohesion principle applicable to European direct tax law, may in the future allow more predictability of results.

4. Relevant objective elements apt to justify a restriction to a fundamental freedom or a discriminatory treatment, resulting from a direct tax regime

In exceptional cases, discriminatory/restrictive tax rules are accepted by the Court, and may therefore be kept by the Member States, as long as they are proportional, on the grounds of specific justifications connected with an "overriding public interest" reason, and interpreted strictly.

As stated above (3.6.), justifications or "relevant objective elements apt to justify a restriction to a fundamental freedom or a discriminatory treatment" constitute a negative limit to the decision of incompatibility of domestic and tax treaties rules in respect of the EC Treaty, and therefore contribute to *acte clair* in direct tax issues.

Even though legitimate public interests are, in principle, only those expressly provided for in the Treaty, in the field of direct taxes the ECJ has developed a concept of overriding public interest that is different from the Treaty provisions on legitimate public interest reasons of public policy, public security and public health (as these are not applicable to direct tax law issues): this concept is basically connected to the prevention of abuse of law in the form of tax avoidance, and to the effectiveness of fiscal supervision, although the exact contours of the allowed justifications are not yet clear[83].

As Van Thiel explains in his contribution to this book[84], the public policy justification could have been interpreted by the Court as covering some tax policy aims, such as the need to ensure revenue or to prevent tax avoidance (and evasion), but it was restrictively interpreted in connection with threats

82. Ana Paula Dourado, "From the Saint-Gobain to the Mettalgesellschaft: scope of non-discrimination of permanent establishments in the EC Treaty and the most-Favoured-Nation clause in EC Member States tax treaties", *EC Tax Review*, 2002, n.° 3, p. 147 et seq.; Vogel/Gutmann/Dourado, "Tax Treaties..., cit., p. 83 et seq.

83. See Peter Wattel, "Fiscal Cohesion, Fiscal Territoriality and Preservation of the (Balanced) Allocation of Taxing Power; What is the Difference", *The Influence of European Law*....cit., p. 139 et seq.

84. "Justifications in Community Law...", cit., point 2.

to public policy affecting fundamental interests of the Member State, and therefore it cannot be used to justify discrimination and nor does it cover tax-related concerns.

4.1. Disparities versus justifications for discrimination/ restrictions

If I adopt a substantive concept of discrimination/restriction, some arguments accepted by the Court explaining disparities in treatment compatible with the EC Treaty should be distinguished from justifications to discrimination/restrictions. In the latter case, the domestic or tax treaty rules are incompatible with the fundamental freedoms provisions of the EC Treaty, and therefore are only exceptionally accepted and must be strictly interpreted. In contrast, in the first case, domestic tax legislation (or tax treaties) contains or leads to "disparities in treatment, for persons and undertakings subject to the jurisdiction of the Community, which result from divergences existing between the various Member States, so long as they affect all persons subject to them in accordance with objective criteria and without regard to their nationality" and the provisions on the fundamental freedoms are not concerned with those (*Shempp*, para. 34). The same occurs in respect of every different treatment applicable to non-comparable situations (cf. *Schumacker*, *Verkooijen*, *Manninen*, *Blanckaert*, *Bouanich*, Art. 58 (1) (a) EC Treaty).

Beyond the aforementioned comparability test, the non-applicability of domestic law to purely domestic situations (*Werner*), the cohesion argument linked to the comparability of Member States or disparities in tax regimes (*N.*, *ACT Group Litigation, FII Group Litigation, Denkavit Internationaal, Scorpio, Gilly, Schempp*), the less favourable regimes resulting from the application to cross-border situations of different domestic tax regimes (*Gilly, Schempp*) or different tax treaties regimes (*D.* and *ACT Group Litigation*), the present state of Community law (*Daily Mail*), even if considered to be *wrong* arguments or disputable ones, are outside the scope of discrimination/restriction and do not constitute justifications to prohibited discriminations/restrictions. On the contrary, in his paper published below, Van Thiel analyses some of these arguments under the concept of justification[85].

85. "Justifications in Community Law...", points 2 and 3; Peter Wattel also considers that the preservation of the balanced allocation of taxing power has been recently introduced by the ECJ as a justification for direct tax restrictions: "Fiscal Cohesion...", cit., pp. 139, 140, 151 et seq.

4.1.1. Art. 58 (1) (a) EC Treaty

Interpretation that has been given by the ECJ of Art. 58 (1)(a) EC Treaty, allowing application of the tax treaties/domestic tax law provisions that distinguish between taxpayers who are not in the same situation with regard to their place of residence or with regard to the place where their capital is invested neutralizes what seemed to be a justification to an infringement to Art. 56. In fact, it results from settled case law, concerning capital movements involving Member States, that either a different treatment is applied to non-comparable situations and therefore there is no discrimination/restriction (*Verkooijen*, paras. 43 to 46, *Maninnen*, para. 29, *Blanckaert*, para. 42, *Bouanich*, para. 38) – and the same reasoning applies to any other cross-border movements (e.g. *Schumacker*, paras. 30-34 and 39)- or a discriminatory/restrictive tax regime is justified by an overriding public interest not different from the ones accepted by the Court in tax matters and in respect of any other fundamental freedoms (*Verkooijen*, paras. 43 to 46, *Manninen*, para. 29, *Blanckaert*, para. 42, *Bouanich*, para. 38). It is true that in some cases the Court uses a confusing method of analysis. For example in *Lenz* the objective difference in the situation is considered to justify a difference in tax treatment and Art. 73 d (1) (currently, Art. 58 (1)) is treated as a whole (para. 28). And in *Manninen* and *Bouanich*, the Court again treats Art. 58 (1) as whole. But in *Maninnen*, even if the Court holds at para. 28 that Art. 58 (1) (a) is a derogation rule, and has to be interpreted strictly (therefore applying the reasoning it applies to any justification), in para. 29, it distinguishes between "situations which are not objectively comparable or be justified by overriding reasons in the general interest". A similar method is used in *Bouanich*, paras. 36 and 38.

So far, the Court has not justified any restrictive direct tax measure involving third states with Art. 58(1)(a), either. Although in *Van Hilten*, *Thin Cap Group Litigation* (cf., in non-tax matters *Fidium Finanz*[86]) and *A.* the ECJ had the opportunity to consider that the situations were covered by Art. 56 but fell under the exception of Art. 58 (1) a), it did not follow that path and Art. 58 (1) (a) was not taken into consideration. The ECJ either considered the situation to be out of the scope of the free movement of capital (*Van Hilten, Fidium Finanz, Thin Cap Group Litigation*) or to be covered under the exception of Art. 58 (1) (b) (see *A.*, paras. 55 et seq.), although it is not clear whether Art. 58 (1) (b) is autonomous from the "effectiveness of fiscal supervision" (see 4.1.2.2.).

86. ECJ, 3 October 2006, Case C-452/04.

4.1.2. Justifications for discrimination/restrictions

Subject to the above preliminary remarks (4.1. and 4.1.1.), in the following pages I will follow Van Thiel's classification of justifications to discriminations/restrictions in direct tax issues[87]:

- Justifications that are either provided by the Treaty but inapplicable to direct tax issues or invoked by the Member States and systematically rejected by the Court;
- Justifications that have been accepted only once by the Court and subsequently rejected or developed in a different direction; and
- Justifications once rejected by the Court and subsequently accepted or accepted in a different context and justifications accepted by the Court.

4.1.2.1. *Justifications that are either provided by the Treaty but inapplicable to direct tax issues or invoked by the Member States and systematically rejected by the Court*

To the first group of justifications belong the public interest reasons of public policy, public security and public health, as they are not adequate to direct tax issues and therefore inapplicable to this area.

Besides, there is settled case law rejecting other justifications in direct tax matters. That is the case of the "effectiveness of fiscal supervision" concerning cross-border situations involving Member States, which, although considered in abstract to be an overriding public interest, has been systematically rejected by the ECJ on the basis that Directive 77/799/EEC on Exchange of Information can assure the aforementioned effective fiscal supervision (*Avoir Fiscal, Bachmann, Schumacker, Maninnen, Futura, Bent Vestergaard, X and Y, Lankhorst-Hohorst, Fournier*)[88]; it is also the case of the "prevention of tax avoidance schemes", either when a Member State tries in this way to justify discriminatory tax regimes, independently of the existence of a wholly artificial arrangement (*Leur-Bloom, Lasteryie du Saillant, Lankhorst-Hohorst, Metallgesellschaft, ICI, Rewe Zentralfinanz, Cadbury Schweppes, Elisa*), and or using connected domestic non-rebuttabble tax presumptions (*Cadbury Schweppes, Tallota,* indirectly, *Elisa*).

However, the ECJ has accepted the effectiveness of fiscal supervision in connection with anti-avoidance/evasion aims, as justifications for discrimi-

87. "Justifications in Community Law...", cit., p. 87 et seq.
88. Servaas Van Thiel, "Justifications in Community Law...", cit., pp. 88-89.

natory/restrictive measures when third states are involved (See *A., FII Group Litigation;* cf. *Van Hilten*).

Measuring, balancing or compensating the disadvantageous effect of the discriminatory measure is also refused by the ECJ as a valid justification (*Avoir Fiscal, Bachmann, Saint-Gobain, Eurowings, Verkooijen, AMID, Biehl, Skandia, Cadbury Schweppes*), although the *Columbus Container* decision disturbs this case law.

The loss/diminution of tax revenue or the coherence of the domestic regime linked to an argument of loss of revenue has been consistently rejected (*Asscher, ICI, Saint-Gobain, Verkooijen, Metallgesellschaft, Danner, Skandia, Eurowings, X and Y, Bent Vestergaard, De Groot, Lasteryie du Saillant, Verkooijen, Lenz, Manninen, Commission v. Portugal, Commission v. Sweden*), although the recent comparison tests created by the Court as well as some other decisions, such as the one in *Columbus Container*, leave some doubts concerning the real relevance given by the Court to this aspect (See the two Advocate General Opinions in *Meilicke*, but also *N., Schempp, Scorpio, Columbus Container, A.*).

4.1.2.2. *Justifications that have been accepted only once by the Court and subsequently rejected or developed in a different direction*

The best example of a justification that has been accepted only once by the Court and subsequently developed in a different direction is the coherence justification used in *Bachmann*. The Court never formally rejected its decision in *Bachmann*, but has systematically refused the coherence justification, with the argument that its applicability requires a direct link between deductibility of expenses/losses and taxability of subsequent income (*Asscher, ICI, Eurowings*), and as Van Thiel argues in this book, "the coherence argument necessarily has a very limited scope in Community law, because it cannot serve as an alternative for the revenue and compensation arguments which the Court has consistently rejected"[89].

89. Servaas Van Thiel, "Justifications in Community Law...", cit., p. 89.

4.1.2.3. *Justifications once rejected by the Court and subsequently accepted or accepted in a different context and justifications accepted by the Court*

On the other hand, the Court developed the coherence argument on a bilateral level and recently enlarged the comparability test to Member States or to the tax regime applicable to the recipient in the case of deduction of maintenance expenses (see *Wielockx, N., Schempp, Scorpio, Manninen, Marks & Spencer, A, Deutsche Shell, ACT Group Litigation, FII Group Litigation*), but this development, according to our understanding and as explained above (4.1.1.), does not constitute a justification.

It is settled case law that the balanced allocation of tax jurisdiction, when linked to the risk of tax avoidance/tax evasion and/or a risk of taking into account tax losses twice, has been invoked as a justification to restrictive tax measures (see *Marks & Spencer*, para. 51, *Rewe Zentralfinanz* para. 41, *Oy AA* paras. 51, 54-59, 60-62).

Abuse of Community law is a principle governing the interpretation of Community law[90] and consequently, as already mentioned above, nationals of Member States cannot abuse Community law in order to circumvent their national legislation: this argument was suggested by Advocate General Darmon in *Daily Mail*, but not mentioned by the Court in its decision, and accepted in *Knoors*, para. 25, *Bouchoucha*, para. 14, *Centros*, para. 24, *Cadbury Schweppes*, para. 35[91]. I also recalled above that the fact that a company exercises its freedom of establishment in a Member State, in order to benefit from more favourable legislation does not necessarily constitute abuse of the freedom (*Barbier*, para. 71; *Centros*, para. 27; *Inspire Art*, para. 96, *Cadbury Schweppes*, paras. 36-37).

In this context, a national measure restricting freedom of establishment was considered to be justified if it specifically relates to wholly artificial arrangements aimed at circumventing the application of the legislation of the Member State concerned (*ICI*, para. 26, *Lankhorst-Hohorst*, para. 37, *De Lasteyrie du Saillant*, para. 50, *Marks and Spencer*, para. 57, *Cadbury Schweppes*, paras. 51, 55-56 and *Thin Cap Group Litigation*, para. 72) or if the risk of organizing such arrangements exist (*Oy AA*, para. 58).

90. See Advocate General Poiares Maduro, Opinion on *Halifax plc.*, points 62-72; and ECJ 21 February 2006, paras. 71-75.
91. See on the subject, Rita de La Feria, "Prohibition of Abuse ...", cit., *WP 07/23*.

Moreover, the ECJ has accepted the effectiveness of fiscal supervision in connection with anti-avoidance/evasion aims, as justifications for discriminatory/restrictive measures when third states are involved (See *A., FII Group Litigation*; cf. *Van Hilten*). And, on the other hand, the Court took a step back in the comparison test in *Columbus Container*, abstaining from comparing the result of the different tax relief rules applicable to the host Member States of the German outbound investment, instead of applying the *Cadbury Schweppes* criteria.

At last but not least, according to Art. 58 (1) (b) Member States are not precluded from taking all requisite measures to prevent infringements of national law and regulations, in particular in the field of taxation. Whereas this justification has not been accepted in cross-border situations involving Member States – neither in respect of the free movement of capital nor in respect of any other fundamental freedoms, unless there is a wholly artificial arrangement -, when third states come into play, the ECJ accepts as relevant the argument of a need for effective fiscal supervision and therefore Art. 58 is also applicable.

In fact, in *A.*, the Court links Art. 58 (1) (b) to its settled case law, according to which the need to guarantee the effectiveness of fiscal supervision constitutes an overriding requirement of general interest capable of justifying a restriction on the exercise of freedom of movement guaranteed by the Treaty (*A.*, para. 55; cf. *Futura*, para. 31, *Lenz*, paras. 27 and 45, *Stauffer*, para. 47). Due to the inapplicability of Directive 77/799/EEC, it considers that it is legitimate for a Member State to refuse to grant an advantage if the third state is not under any contractual obligation to provide information and it proves impossible to obtain such information from that country (para. 63).

5. Temporal effects of an ECJ decision

ECJ decisions have, as a rule, retroactive effects, and accordingly, a tax regime considered to be incompatible with the fundamental freedoms in a preliminary ruling cannot be applied by a national court in respect of legal relationships arising and established either after or before the ruling (*Defrenne*[92], *Denkavit Italiana*[93], *Meilicke*, para. 37[94]).

92. ECJ, 8 April 1976, Case 43/75, *Defrenne*.
93. ECJ, 27 March 1980, Case 61/79, *Denkavit Italiana*.
94. Cf. on the issue, Juha Raitio, *The Principle of Legal Certainty in EC Law*, Dordrecht, 2003, pp. 196-199.

There are two limits to this rule in tax matters, as Frans Vanistendael reminds us in his paper[95]: The taxpayer must respect the national statute of limitation in claiming a refund (although that statute may not make such refund effectively impossible – *Denkavit Italiana*, paras. 25-28); And the taxpayer must prove that he has incurred an effective damage by paying the tax that was not legally due, and that he has not shifted the tax burden to another person (*Francovich*[96]).

Exceptionally, the ECJ may restrict the temporal effects of its rulings - the ECJ has the exclusive competence to do it - and some requirements can be considered to be settled case law, even if some others are not yet clear (and these are highlighted by Michael Lang [97]).

One of the requirements, which is connected with Art. 234 EC Treaty and the *CILFIT* criteria, is the previous inexistence of a preliminary ruling on a legal point of law – the non-existence of *acte clair* or, instead, of *acte éclairé*, if we accept the difference between both.

In other words, there is a principle, according to which only in the actual judgment ruling upon an interpretation on a point of law may there be a restriction to temporal effects (*Barra*[98], para. 13; *Vincent Blaizot*[99], para. 28; *Legros and Others*[100], para. 30; *Bosman and Others*[101], para. 142; *EKW* and *Wein and Co.*[102], para. 57, *Meilicke*, para. 62[103]).

This means that if there has been a ruling upon an interpretation on a point of law in which the ECJ decided not to restrict the temporal effects, all subsequent rulings on the same or similar issue will be unrestricted in their temporal effects (see *Meilicke*).

Alternatively, if there has been a ruling upon an interpretation on a point of law in which the ECJ decided to restrict the temporal effects, the subsequent rulings on the same or similar issue will have temporal effects retroactive to the date of the first relevant ruling.

95. "Consequences of the Acte Clair…", cit., p. 160
96. ECJ, 19 November 1991, Joined Cases C-6/90 and C-9/90, *Francovich and Others*.
97. See on the unclear issues, Michael Lang, "Acte Clair and Limitations of the Temporal Effects of ECJ Judgments", points 4-5.
98. ECJ, 2 February 1988, Case 309/85, Barra.
99. ECJ, 2 February 1988, Case 24/86, *Blaizot*.
100. ECJ, 16 July 1992, Case C-163/90, *Legros*.
101. ECJ, 15 December 1995, Case C-415/93, *Bosman*.
102. ECJ, 9 March 2000, Case C-437/97, *Evangelischer Krankenhausverein Wien*.
103. ECJ, 6 March 2007, Case C-292/04, *Wienand Meilicke*.

In *Meilicke*, the Court considered that the first judgment on non- discrimination of inbound dividends was *Verkooijen* (para. 33), being implicitly irrelevant for this purpose whether dividends were domestically exempted (*Verkooijen*, *Lenz*), or taxed but benefiting from an imputation credit (*Manninen* and *Meilicke*).

It can then be deduced, under the *CILFIT* doctrine, that domestic courts could have abstained from referring a case on inbound dividends in *Lenz*, *Manninen* and *Meilicke* (see also *FII Group Litigation*, para. 215), but for them this was not clear, as there are also good arguments to consider that the situation was clear not from *Verkooijen* on, but rather since *Manninen*, as the *Finanzgericht Köln* argues in *Meilicke*.

In fact, the point of law in *Meilicke* is closer to *Manninen* than to *Verkooijen*, as in *Manninen* the Court had to consider whether the home Member State had to take into account the domestic tax law of the host Member State (see above, 3.7.4., concerning the reshaping of the territoriality principle). As Michael Lang writes in his paper, it is extremely difficult for taxpayers and governments to know what level of abstraction the ECJ would choose (i.e. the one regarding treatment of inbound dividends, or the one regarding treatment of inbound dividends by Member States applying the credit method)[104]. As governments have to ask for a limitation of temporal effects in time, the ECJ solution implies that it is safer that a Member State always tries to get that temporal limitation.

Had the Court limited the temporal effects in *Verkooijen*, all subsequent preliminary rulings on an identical or similar and clear point of law – *Lenz*, *Manninen*, *FII Group Litigation* and *Meilicke* – would have their temporal effects limited to the date of the ECJ judgment on *Verkooijen*, although the claims that have been brought before that date would benefit from the interpretation by the ECJ (see, however, the different proposals for cut-off dates, of Advocate General Tizziano[105] and of Advocate General Stix-Hackl in their Conclusions in *Meilicke*[106]).

The identification of the ECJ ruling that creates the precedent and may therefore exceptionally limit the temporal effects of the judgment is not a formal requirement merely linked to the *acte clair* doctrine or to *CILFIT*.

104. "Acte Clair and Limitations…", cit., p. 154.
105. Advocate General Tizziano, Opinion delivered on 5 October 2005, Case C-292/04, *Meilicke*, point 62.
106. Advocate General Stix-Hackl, Opinion delivered on 5 October 2006, Case C-292/04, *Meilicke*, point 38.

On the contrary, it is closely connected to the guiding requirement on the limitation of temporal effects, i.e. to the "general principle of legal certainty inherent in the Community order" (*Defrenne, Vicent Blaizot, Légros and Others, EKW* and *Wein, Meilicke*), which is applicable as long as the legal relationships established under the provisions interpreted were established in good faith. In other words, the fact that the ECJ is called for the first time to interpret a Community provision is not sufficient for assuming legal uncertainty (*Société Bautiaa*[107], *Athinaiki Zythopoiia*).

The assessment of legal certainty depends on the effects of the provisions interpreted by the Court on which the authorities and any other persons concerned relied upon.

And it is worth stressing that this legal certainty results from the uncertainty on the compatibility with EC law of the provision being interpreted. For example in *Légros and Others*, the "dock dues" imposed in the French overseas departments were held by the ECJ to be prohibited customs duty applicable to goods moving between Member States. According to the Court, until that judgment, "the specific identity of the French overseas departments and the particular characteristics of the dock dues have created a situation of uncertainty regarding the lawfulness of the charge at issue under Community Law" (para. 30). That uncertainty was reflected by the conduct of the Community institutions, which led the French Republic and the local authorities in the French overseas departments reasonably to consider that the applicable national legislation was in conformity with Community law (paras. 31-33). "Overriding considerations of legal certainty preclude legal relationships whose effects have been exhausted in the past from being called into question, which would retroactively upset the system for financing the local authorities concerned" (para. 34).

When asking for a limitation of temporal effects of a ruling, Member States normally refer to the "disastrous financial consequences" resulting from repayment of unduly paid amounts and when the Court accepted restricting those effects, the financial argument was often taken into account, although the situation was not examined in detail. In *Defrenne* (and in *Bosman*) those consequences would affect private undertakings/entities and in other cases, public entities (*Defrenne*, para. 70, *Légros and Others*, para. 29; *Blaizot* para. 34; *EKW*, para. 59, *Sürül*[108], para. 111). But in *Bosman*, for example the Court, in spite of limiting the temporal effects of its judgment, on the

107. ECJ, 13 February 1996, Case C-197/94, *Société Bautiaa*.
108. ECJ, 4 May 1999, Case C-262/96, *Sürül*.

basis of the legal certainty argument, did not examine the issue of possible economic consequences (see para. 17).

In any case, the "disastrous financial consequences" have only been considered a relevant argument when linked to the criterion of legal certainty. Autonomously considered, the financial consequences do not seem to justify limiting the temporal effects of a judgment (*Société Bautiaa*; *Athinaiki Zythopoiia*), although the ECJ has also argued that the referring Member State "has not been able to demonstrate the soundness of the calculation which led it to argue before the Court that the present judgment might, if its temporal effects were not limited, entail significant financial consequences". And it is not up to the Court to examine how severe the economic consequences of its judgments are, the burden of proof being with the governments of the Member States (*Stradasfalti*[109]; cf. *Bidar*[110]).

6. Damages and liabilities

In *Brasserie du Pêcheur* and *Factortame* [111] (para. 32), *Konle*[112] (para. 62) and *Haim*[113] (para. 27), the Court recognized that the principle of state liability in case of breach of the EC Treaty applies to any case in which a Member State breaches Community law, independently of the authority of the state whose act was responsible for the breach[114].

In *Köbler*, the ECJ expressly recognized the possibility of state liability in case a national court breaches the EC Treaty fundamental freedoms, and considered it as part of the general principle of liability of a Member State for damage caused to individuals as a result of breaches of Community law for which the state is responsible (*Köbler*, para. 30; see also, *Francovich and Others*, para. 35; *Brasserie du Pêcheur* and *Factortame*, para. 31; and others cited at para. 30 of *Köbler*). According to the Court, the principles of *res judicata*, independence and authority of the judiciary are not disputed (*Köbler*, paras. 38-43), but the right to reparation for damages opens the possibility of litigation involving the same issue[115].

109. ECJ, 14 September 2006, *Case* C-228/05, *Stradasfalti Srl.*
110. ECJ, 15 March 2005, Case C-209/03, *Dany Bidar.*
111. Joined Cases C-46/93 and C-48/93 *Brasserie du Pêcheur and Factortame.*
112. ECJ, 1 June 1999, Case C-302/97 Konle.
113. ECJ, 4 July 2000, Case C-424/97, Haim.
114. See Takis Tridimas, *The General Principles...*, cit., pp. 502-503.
115. Takis Tridimas, *The General Principles...*, cit., p. 528; Peter Wattel, "Köbler, CILFIT and Welthgrove: we can't go on meeting like this", *Common Market Law Review*, 2004, p. 177.

Moreover, the Court recalled that the obligation of national courts under Art. 234 (3) of the EC Treaty aims at preventing infringement of individual rights as conferred by Community law (*Köbler*, para. 35).

Para. 51 of the *Köbler* case enumerates 3 conditions "to be satisfied for a Member State to be required to make reparation for loss and damage caused to individuals as a result of breaches of Community law for which the State is responsible (...): the rule of law infringed must be intended to confer rights on individuals; the breach must be sufficiently serious; and there must be a direct causal link between the breach of the obligation incumbent on the State and the loss or damage sustained by the injured parties".

The ECJ has recognized that the first condition is fulfilled where there is a breach of a fundamental right (paras. 23 and 54 of the *Brasserie du Pêcheur* and *Factortame;* para. 211 of the *FII Group Litigation*; and para. 116 of the *Thin Cap Group Litigation*). As to the second condition – the seriousness of the infringement – it occurs where it is manifest ("State liability for an infringement of Community law by a decision of a national court adjudicating at last instance can be incurred only in the exceptional case where the court has manifestly infringed the applicable law", *Köbler* case, para. 53; see para. 56). The degree of clarity and precision of the rule infringed, as well as the non-compliance by the national court with its obligation to make a reference under Art. 234 (3) of the EC Treaty (*Köbler* (para. 55), or to previous and clear case law (*Brasserie du Pêcheur* and *Factortame*, para. 57, *FII Group Litigation*, para. 214, *Thin Cap Group Litigation*, para. 120) are factors, among other ones (whether the infringement was intentional, whether the error of law was excusable), that contribute to determine whether the breach is sufficiently serious (and it will be considered to be sufficiently serious if the decision is in manifest breach of Community law) – *Köbler*, paras. 55 and 56.

The aforementioned combination of *Köbler* and *CILFIT* has led to two analyses, in opposite directions. One possible interpretation of *Köbler* is that, taking into account that in direct tax issues, as well as in other fields, it is hard to decide when the position of the ECJ is clear, if national courts of last instance want to avoid the risk of making the state liable, it is advisable for them to ask for a preliminary ruling (otherwise, they should be exempt from liability)[116]. Basically, since the ECJ case law is itself unclear and therefore

116. Takis Tridimas, *The General Principles...*, cit., p. 525; Peter Wattel, "Köbler, CILFIT and Welthgrove...", cit., p. 178; Paul Craig and Gráinne de Búrca, *EU Law...*, cit., p. 479; Advocate General Stix-Hackl, Opinion on *Intermodal Transports BV*, point 106.

does not allow national courts to follow the *CILFIT* conditions, the cross reference to *CILFIT* in *Köbler* can have dangerous consequences for national courts. But if national courts are going to increase their referrals to the ECJ in order to avoid state liability, the workload at the ECJ will also increase. Thus, *Köbler* encourages more preliminary references[117]. Besides, even though assuming that to entrust a court with the task of determining whether its own conduct is unlawful is contrary to Art. 10 of the EC Treaty[118], it is up to the Member States to decide which national court is competent to judge the infringement of EC law by another national court that did not, but should have, referred a case to the ECJ, and to refer a case to the ECJ in order to certify whether there was an infringement[119].

Another reading of *Köbler* is that state liability due to national courts infringement of Community law will seldom occur, since, in *Köbler*, the ECJ decided that the infringement was not manifest, in spite of the fact that the Court considered that the Austrian *Verwaltungsgerichtshof* ought to have maintained its request for a preliminary ruling instead of withdrawing it (paras. 117-119)[120]. *Commission v. Italy*[121] was the first infringement action (ex Art. 226 EC Treaty) regarding whether the exercise of the right to repayment of charges levied in breach of Community rules was made excessively difficult for the taxpayers, and was directed towards national courts (the effect of the national provision subject of different relevant judicial constructions "must be determined in the light of the construction which the national courts give to it" (para. 31)). But the ECJ finally adopted a solution that avoids the difficulties of *Köbler* by holding that the Italian legislator (and not its courts) was liable for adopting a provision that enabled national courts to ultimately breach EC law (para. 41).

However, in *Traghetti*[122], the ECJ does not really clarify *Köbler*, since the Court was still rather vague, when it held that Community law "precludes national legislation which limits State liability solely to cases of intentional fault and serious misconduct on the part of the court, if such a limitation were to lead to exclusion of the liability of the Member State concerned in

117. Takis Tridimas, *The General Principles...*, cit., p. 525; Peter Wattel, "Köbler, CILFIT and Welthgrove...", cit., p. 180-181.
118. Advocate General Léger, Opinion delivered on 3 February 1998, ECJ Case C-185/95 P, *Baustahlgewebe*.
119. ECJ, 16 December 1976, Case 33/76, *Rewe*; ECJ, 16 December 1976, Case 45/76, *Comet*; Peter Wattel, "Köbler, CILFIT and Welthgrove...", cit., p. 180.
120. See, Daniel Sarmiento, "Los 'Free-Lance'...", cit., pp. 417 et seq., 422-425.
121. ECJ, 9 December 2003, Case C-129/00.
122. ECJ 13 June 2006, Case C-173/03.

other cases where a manifest infringement of the applicable law was committed, as set out in paragraphs 53 to 56 of the *Köbler* judgment" (para. 46).

Taking into account the ECJ case law on damages and liability, it can be added that the *CILFIT* criteria would not imply an exaggerated shift in favour of national courts regarding the competence to interpret EC law if the ECJ were clearer in respect of its "new policies, the progression in its views, and its regrets or abandonment of earlier cases"[123] and if the three *Köbler* conditions were in effect applicable to national courts.

But *Köbler* and *Traghetti* themselves raise too much uncertainty. *Kühne & Heitz NV*[124] (regarding revision of administrative decisions on the basis of new case law of the ECJ, limited to addressees who previously appealed against the decision up to the last instance, but were rejected), could seem easier to apply than *Köbler*, because the condition of "manifest infringement" of EC law is not required. However, as Sarmiento argues, it is also difficult for national courts to fulfil all requirements imposed by the *Kühne & Heitz* decision and due attention must further be paid to cases such as *i-21*[125], *Kempter*[126], *Kapferer*[127] and *Lucchini*[128].

And above all, still following Sarmiento[129], EC remedies are the litigant's last course of action, which can be used only when all ordinary remedies have been exhausted. Such a subsidiary source of satisfaction in the protection of European rights is costly and lengthy and therefore not the ideal one.

7. The interpretation of the *acte clair* doctrine by the courts in the EC Member States

Considering the interpretation of the *CILFIT* doctrine by the national courts, as reported in this book, I can reach the broad conclusion that the main problem constitutes the lack of justification when supreme courts or tribunals deciding in last instance do not refer a case on the basis of *acte clair* (on the basis of no reasonable doubt on how to solve a case). The authors in this book also agree that the number of cases on direct tax issues referred by

123. Peter Wattel, "Köbler, CILFIT and Welthgrove…", cit. p. 179
124. ECJ, 13 January 2004, Case C-453/00.
125. ECJ, 19 September 2006, Joined Cases C-392/04 and C-422/04.
126. ECJ, 12 February 2008, Case C-2/06.
127. ECJ, 16 March 2006, Case C-234/04.
128. ECJ, 18 July 2007, C-119/05; See, Daniel Sarmiento, "Who's Afraid…?", cit. p. 79.
129. Daniel Sarmiento, Id., p. 79.

their national courts is lower than what would result from a correct interpretation of the *CILFIT* criteria (therefore, the relatively low number of cases referred to the ECJ in direct tax issues has not contributed much to the overload of work at the ECJ).

The exact number of cases that were not, but should have been, submitted to the ECJ, according to a correct interpretation of *CILFIT* would give us an accurate diagnosis on the attitude of national courts towards the preliminary ruling procedure. Unfortunately, that number is not possible to identify, as there is no central database keeping a continuous track of the issue – the ECJ itself does not have a complete one yet and access to the existing one is restricted.

It seems as though the aforementioned aspects are connected: the lack of justification contributes to hiding non-referred cases that do not correctly fulfil the *CILFIT* criteria and, what is more, does not allow us to know what is the real underlying motivation (whether it is driven by protection of national revenue or anti-abuse concerns, for example). A rule obliging national courts to justify why they do not refer some cases to the ECJ would, on the one hand, reduce some of those non-referred decisions and, on the other hand, improve the results targeted by *CILFIT*, i.e. contribute to the construction of a vertical system of cooperation between the national courts and the ECJ, a decentralized system of legal protection as argued in *Kühne & Heitz NV* and Advocate General Stix-Hackl in *Intermodal* (C-495/03, paras. 104, 107, 121,122).

I can therefore argue that currently the *acte clair* doctrine leads to a shift in favour of national tax courts, of the ultimate power of interpretation of European law, which is not used in a completely correct way, basically due to the lack of an obligation to justify non-referrals and to the difficult application of state liability as it results from the *Köbler* criteria.

As Sousa da Câmara and Zalasinski highlight in their papers, until the *Avoir Fiscal* case, it was not certain whether the fundamental freedoms were applicable to direct tax issues[130], and most of the papers published in this book seem to agree that in direct tax issues, in the absence of harmonization, it is difficult to argue that *acte clair stricto sensu* (in the sense of para. 16 of *CILFIT*) exists, unless there is settled case law (*acte éclairé*, in the sense of para. 14 of *CILFIT*, for those who accept the autonomy of paras. 14 and

130. Francisco de Sousa da Câmara, "The Meaning and Scope …", cit., p. 373; Adam Zalasinski, "Acte Clair, Acte Éclairé…", cit., p. 336.

16). However, for example in some of the domestic cases described by Weber/Davits, the Netherlands Supreme Court uses the *acte clair* argument of "no reasonable doubt" – "there is no reasonable doubt" – in order to deny a referral to the ECJ[131]. One of these cases concerned the domestic treatment given to inbound dividends, more specifically whether the foreign withholding tax could be credited in the Netherlands against the corporate income tax that X NV was due. The Netherlands Supreme Court considered that there was no reasonable doubt that the issue was not covered by the freedom of establishment. Besides the fact that, according to Weber/Davits[132] (6.2.1.), the Court did not give its reasoning for the decision, it must be stressed that the issue of the overlap of freedoms when third countries are involved, was not clear until recently – see, for example the *FII Group Litigation* and *Holböck*. The purpose test as used in these two cases could have led to a different result in the aforementioned Dutch case on foreign withholding tax, involving third states. Other Dutch cases, such as, for example an exit tax due to the change of residence of a company (taxation of hidden reserves), non-deduction of mortgage interest for a primary home outside the Netherlands, refusal to exempt from capital duty on the basis of *fraus legis*, were considered to be *acte clair stricto sensu* although the state of Community law (including ECJ case law) was not taken into account[133]. As I initially argued – and the Dutch cases reported by Weber/Davits confirm – *acte clair* and interpretation of settled case law are related and have to be jointly applied.

Beyond these broad conclusions, the attitude of national courts towards Art. 234 of the EC Treaty varies significantly.

For example according to the Austrian report, one of the reasons for the reduced number of Austrian referrals is the absence of some "specific regimes found in other sophisticated ones, for various tax policy reasons"[134]. Moreover, although there have been only three referrals to the ECJ, there is a high success rate of taxpayers in Austrian courts regarding EC law issues and even in cases where *CILFIT* is not applied correctly.

Occasionally, the Portuguese tax courts also apply the ECJ case law (see the reference to the thin capitalization rules considered to be incompatible with the EC Treaty on the basis of the *Lankhorst-Hohorst* ruling, by a Portuguese tax court), but have not gone as far as the Swedish courts, which frequently implement the ECJ case law without domestic legal grounds when it is favourable to the taxpayer (and have discussed whether this would be acceptable if the decisions were not favourable to the taxpayer)[135]. Besides, the Swedish Board of Advance Rulings (which is not a court for the purpose of Art. 234 of the EC Treaty) has played an important, dynamic role in Sweden, as it has jurisdiction to deliver binding preliminary decisions on the application of tax law, and its decisions may be challenged in the Supreme Administrative Court[136]. By contrast, Portuguese taxpayers (and especially individuals) often choose not to claim the incompatibility of domestic tax rules with the fundamental freedoms before the national courts, as they find that path is of uncertain outcome, as well as expensive and long[137].

131. "The Practical Application...", cit., p. 299.
132. Idem, point 6.2.1.
133. Ibid., points 6.2.2.-6.2.4.
134. Georg Kofler, "Acte Clair, Community Precedent...", cit., p. 177.

Spanish courts have also occasionally applied the ECJ case law to thin capitalization rules, but García Prats characterizes the use of the *acte clair* doctrine by the Spanish Supreme Court as often wrong, insufficient and worrying[138]. The almost complete absence of direct tax cases referred by the Italian courts contrasts to what is happening in the VAT domain and in respect of (possibly) abusive tax schemes, the latter requiring interpretation of (indeterminate) principles[139]. The Polish attitude of the administrative courts towards *CILFIT* is still uncertain, and as they have the duty to take into account *ex officio* all relevant problems connected to EC law, it is expected that they correctly apply the preliminary ruling procedure.

Common attitudes to some of those courts can also be found. For example in Austria, in the Netherlands and in Sweden, national courts have been increasingly extending the ECJ's reasoning, on the basis of ECJ previous case law: Austrian courts have extended the ECJ reasoning in the *Lenz* case, to dividends from the EU and EEA companies and to other types of cross-border capital income, including interest payments[140]. It is also worth mentioning that in Sweden and in Portugal, the infringement procedures initiated by the Commission have often led to amendments of the tax legislation[141].

135. Francisco de Sousa da Câmara, "The Meaning and Scope ...", cit., p. 381 ; Cécile Brokelind, "The Acte Clair Doctrine...", cit., point 5.
136. Cécile Brokelind, "The Acte Clair Doctrine...", cit., p. 482.
137. Francisco de Sousa da Câmara, "The Meaning and Scope ...", cit., p. 385.
138. Alfredo García Prats, "The Acte Clair Doctrine...", cit., p. 444.
139. Pasquale Pistone, "The Search for Objective Standards...", cit., point 1.4.
140. Georg Kofler, "Acte clair, Community Precedent...", cit., p. 193.
141. Cécile Brokelind, "The Acte Clair Doctrine...", cit., p. 456; Francisco de Sousa da Câmara, "The Meaning and Scope...", cit., point 3.1.

8. Conclusions

Our research was aimed at analysing the meaning and scope of the *acte clair* doctrine in direct tax issues, and at searching for standards guiding national courts or tribunals of last instance in the application of Art. 234 (3) EC Treaty and the *CILFIT* criteria. The conclusions I reach in this general report depart from the arguments and results achieved in the other papers published in this book, but do not necessarily reflect the opinion/conclusions expressed by the authors of those papers.

Most of the authors in this book accept the distinction between *acte éclairé* (para. 14 of *CILFIT)* and *acte clair* (first part of para. 16 of *CILFIT*), but expressly or implicitly consider that, in direct tax issues, a national court or tribunal of last instance is only exempt from the obligation to refer a case to the ECJ under Art. 234, when there is settled case law on the issue (i.e. when there is *acte éclairé*).

In direct tax law issues, considering that in the absence of comprehensive harmonization application of the *CILFIT* criteria involves interpretation of the fundamental freedoms, it is for the ECJ to progressively reduce the vagueness of the latter. The inherent vagueness of the Treaty principles on the fundamental freedoms demands constructive interpretation by the Court, and it is hard to think of *acte clair* without previous case law.

If we reject the assertion "*in claris non fit interpretatio*", take into account that the Court is not bound to a *stare decisis* rule and also that interpretation is unavoidable, it should be stressed that paras. 14 and 16 to 20 of the *CILFIT* decision are closely interrelated, and that a national court of last instance is not obliged to refer a case when it considers that there is *no reasonable doubt* on the (in)compatibility of the domestic or tax treaty rule in light of the EC Treaty. This assessment will be made on the basis of the degree of development of case law (i.e. take into account the state of evolution of Community law), and in respect of Art. 10 EC Treaty, but it cannot be determined how many ECJ decisions are necessary to eliminate that reasonable doubt, necessary discretion being left to national courts.

In any case, the *CILFIT* criteria result from teleological interpretation of Art. 234 (3) *EC Treaty* and therefore do not confer powers to national courts that go beyond the aforementioned article, although the opinions in this book, of the Advocates General and in the literature on the subject are far from being unanimous on this issue.

Some national courts are more reluctant to refer cases in respect of non-harmonized matters than in respect of harmonized ones, which may lead us to the broad conclusion that in the absence of *CILFIT* we would probably not have more references to the ECJ in direct tax issues.

According to settled case law, it is possible to conclude that the incompatibility resulting from discriminatory or restrictive tax measures based on the difference between residents and non-residents or taking into account the source state of income (home state v. host state) occurs in respect of different kinds of rules: rules on the tax incidence, tax base, tax rates, anti-abuse, presumptions and procedural rules.

It is however still disputable, due to the absence of case law on the issue, whether non-harmonized definitions of taxpayer and tax object come into the scope of the ECJ's analysis, and it can be argued that they belong in a broad sense to the allocation of taxing rights rules and are still within the competence of the Member States, as long as they do not lead to restrictions incompatible with the fundamental freedoms.

Member States retain the power to define, unilaterally or by treaty, rules allocating tax jurisdiction, such as connecting factors, criteria with a view to eliminating double taxation, regimes aimed at preventing avoidance and evasion. Nevertheless, they should not be discriminatory/restrictive, but the case law is not consistent in this respect. It is not clear either to what extent allocation-of-taxing-rights rules in tax treaties are outside the scope of the EC Treaty. Nor is it clear whether and to what extent rules in double taxation conventions compensate for the discriminatory/restrictive treatment of domestic tax laws.

The ECJ has enlarged the comparison tests and they currently cover the comparison between residents and non-resident taxpayers, the comparison between the tax advantage granted in favour of a shareholder and the tax payable by way of corporation tax, the comparison between the host and the home states (in some situations) and the comparison of the situation of the recipient of the taxpayer's deductible amounts. This methodology of the Court seems to favour an integrated perspective of the taxpayer's situation in the internal market but still needs to be improved in order to gain some consistency and coherence.

Non-comparable situations, the accepted justifications for discriminatory/restrictive measures and non-acceptance of a MFN clause can be con-

sidered negative limits to the assessment of the Court on the compatibility of tax regimes with the fundamental freedoms.

The ECJ is also reshaping the (domestic) tax law principles: the ability-to-pay, the net income taxation, the prohibition of abuse of tax law, all of which have been thought of in the context of the principle of territoriality and are being redefined in the light of the internal market requirements of non-discrimination and prohibition of restrictions. The same reasoning applies to accepted exceptions to discriminatory and restrictive measures. The prevention of inter-state tax avoidance schemes as well as the need for effective fiscal supervision was drafted by the Member States in close connection with the territoriality principle, and is being redefined by the Court. Prevention of tax avoidance schemes has been accepted by the ECJ in line with its general principle of prohibition of abuse, which is connected to the existence of a wholly artificial arrangement, whereas fiscal supervision can be ensured by the EC Directive on exchange of information, unless in the case of free movement of capital involving third states.

It is possible therefore to identify specific types of tax rules in respect of which there is a coherent reasoning and orientation of the ECJ case law, and which can, in this sense, guide the national courts obligation to refer a case to the ECJ. Another connected issue is whether increasing the degree of detail of the case law – for example in respect of tax base rules, such as tax treatment of inbound dividends, tax losses or costs, or in respect of domestic anti-abuse clauses – leads to more legal certainty or not (or rather to less legal certainty) and therefore whether self-restraint by both the ECJ and the national courts is advantageous also in non-harmonized (direct) tax issues (in *CILFIT* and in the *Opinions of Advocates General* recommending self-restraint of the national courts very detailed harmonized rules were the object of the preliminary rulings).

Because under Art. 234 EC Treaty, the ECJ has been asked to interpret the compatibility of different types of very concrete tax rules and tax regimes with the fundamental freedoms, the Court has adopted a step-by-step approach without constructing second-level principles (with the exception of the general principle of abuse). The comparability tests recently enlarged by the Court, aimed at constructing a cohesion principle of second-level applicable to European direct tax law may in the future allow higher predictability of results.

It is not disputed though, that it is possible to reach *acte clair* (or *acte éclairé*, for those who accept the difference) in direct tax issues, in spite of the inherent indeterminacy of the fundamental principles applied by the Court. The Court itself recognizes that possibility, when it exceptionally allows restricting the temporal effects of its rulings, as long as no previous preliminary ruling on a legal point of law exists, and it has applied the same reasoning to a direct tax case. In other words, one case on a legal point of law may be enough for domestic courts abstaining from referring a case in direct tax issues. The identification of the ECJ ruling that creates the precedent and may exceptionally limit the temporal effects of the judgment is not a formal requirement, exceptionally linked to *CILFIT*, but is closely connected to the guiding principle on the limitation of temporal effects: "the general principle of legal certainty inherent in the Community order". Temporal effects may be exceptionally limited, as long as there is no *acte clair* on the issue.

The degree of clarity of the rule infringed as well as the non-compliance by the national court with its obligation to make a reference under Art. 234 (3) EC Treaty or to previous and clear case law can lead to State liability. This could lead us to the conclusion that *Köbler* would encourage more preliminary references. However, the papers published in this book do not seem to confirm that reading of *Köbler*. The main problem regarding interpretation of the *CILFIT* criteria by the national courts concerns the lack of justification when national courts of last instance do not refer a case, because it contributes to hiding non-referred cases that do not correctly fulfil the *CILFIT* criteria and does not allow us to understand the underlying motivation. Besides, it is not possible to identify the exact number of direct tax cases that were not, but should have been submitted to a preliminary ruling. It is possible to find common attitudes of the national tax courts towards *CILFIT* (such as extending the ECJ's reasoning to similar but not identical cases), but they still vary significantly.

All in all, I can conclude that, if national courts comply with Art. 10 EC Treaty when applying the *CILFIT* criteria, if the ECJ develops second and third level principles when applying the fundamental freedoms to direct tax issues, if it pays due attention to the coherence of its rulings or expressly justifies changes in its case law, the advantages of the *CILFIT* doctrine overcome the disadvantages. The aforementioned direct tax issues in respect of which there is settled case law or where it is being developed, with multilateral effects, confirm this optimistic reading of *CILFIT*.

I am convinced that the readers of this book will benefit from the various opinions on the subject published here and have the opportunity to develop their own.

Enjoy your reading!

Annex I: Above Mentioned Direct Tax Decisions of the European Court of Justice (chronological order)

28 January **1986**, Case 270/83 (Commission v French Republic ['**Avoir fiscal**']); 27 September 1988, Case 81/87 (The Queen v ... **Daily Mail** and General Trust plc); 8 May **1990**, Case 175/88 (**Biehl** v Administration des Contributions du Grand-Duché de Luxembourg); 28 January **1992**, Case C-204/90 (**Bachmann** v Belgian State); 26 January **1993**, Case C-112/91 (**Werner** v Finanzamt Aachen-Innenstadt); 13 July 1993, Case C-330/91 (The Queen v ... **Commerzbank** AG); 14 February **1995**, Case C-279/93 (Finanzamt Köln-Altstadt v **Schumacker**); 11 August 1995, Case C-80/94 (**Wielockx** v Inspecteur der Directe Belastingen); 14 November 1995, Case C-484/93 (**Svensson** and Gustavsson v Ministre du Logement et de l'Urbanisme); 27 June **1996**, Case C-107/94 (**Asscher** v Staatssecretaris van Financiën); 15 May **1997**, Case C-250/95 (**Futura** Participations SA and Singer v Administration des contributions); 17 July 1997, Case C-28/95 (**Leur-Bloem** v Inspecteur der Belastingdienst/Ondernemingen Amsterdam 2); 28 April **1998**, Case C-118/96 (**Safir** v Skattemyndigheten i Dalarnas Län); 12 May 1998, Case C-336/96 (**Gilly** v Directeur des Services Fiscaux du Bas-Rhin); 16 July 1998, Case C-264/96 (Imperial Chemical Industries plc [**ICI**] v K. Hall Colmer [Her Majesty's Inspector of Taxes]); 29 April **1999**, Case C-311/97 (**Royal Bank of Scotland** plc v Elliniko Dimosio [Greek State]); 14 September 1999, Case C-391/97 (**Gschwind** v Finanzamt Aachen-Außenstadt); 21 September 1999, Case C-307/97 (Compagnie de **Saint-Gobain** v Finanzamt Aachen-Innenstadt); 14 October 1999, Case C-439/97 (**Sandoz** GmbH v Finanzlandesdirektion für Wien, Niederösterreich und Burgenland); 26 October 1999, Case C-294/97 (**Eurowings** Luftverkehrs AG v Finanzamt Dortmund Unna; 28 October 1999, Case C-55/98 (Skatteministeriet v Bent **Vestergaard**); 18 November 1999, Case C-200/98 (X AB & Y AB v Riksskatteverket); 13 April **2000**, Case C-251/98 (C. **Baars** v Inspecteur der Belastingdienst Particulieren/Ondernemingen Gorinchem); 16 May 2000, Case C-87/99 (**Zurstrassen** v Administation des Contributions Directes); 6 June 2000, Case C-35/98 (Staatssecretaris van Financiën v **Verkooijen**); 14 December 2000, Case C-141/99 (**AMID** v Belgian State); 8 March **2001**, Cases C-397/98 and C-410/98 **Metallgesellschaft** Ltd a.o. v Commissioners of Inland Revenue, H.M. Attorney General); 12 September 2002, Case C-431/01, **Mertens** [order]; 4 October 2001, Case C-294/99 (**Athinaiki** Zithopiia AE v Elliniko Domision [Greek State]); 3 October 2002, Case C-136/00 (**Danner**); 5 November 2002, Case C-208/00 (**Überseering** BV v Nordic Construction Company Baumanagement GmbH (NCC)); 21 November 2002, Case C-436/00 (**X and Y** v Riksskatteverket); 12 December 2002, Case C-385/00 (**De Groot** v Staatssecretaris van Financiën); 12 December 2002, Case C-324/00 (**Lankhorst-Hohorst** v Finanzamt Steinfurt); 12 June **2003**, Case C-234/01 (Arnoud **Gerritse** v Finanzamt Neukölln-Nord); 26 June 2003, Case C-422/01 (**Skandia**, Ramstedt v Riksskatteverket); 18 September 2003, Case C-168/01 (**Bosal** Holding v Staatssecretaris van Financiën); 13 November 2003, Case Case C-209/01 (Theodor **Schilling**, Angelika Fleck-Schilling v Finanzamt Nürnberg-Süd); 11 December 2003, Case C-364/01 (**Barbier** v Inspecteur van de Belastingdienst Particulieren/Ondernemingen Buitenland); 4 March 2004, Case C-334/02 (**Commission v France**); 11 March 2004, Case C-9/02 (**Lasteyrie du Saillant** v Ministère de l'Economie, des Finances et de l'Industrie); 8 June 2004, Case C-268/03 (Jean-Claude **De Baeck** v. Belgische Staat); 1 July 2004, Case C-169/03 (Florian W. **Wallentin** v Riksskatteverket); 15 July 2004, Case C-315/02 (Anneliese **Lenz** v Finanzlandesdirektion für Tirol); 15 July 2004, Case C-242/03 (Ministre des Finances v Jean-Claude **Weidert**, Élisabeth Paulus) ; 7 September 2004, Case C-319/02 (Petri Mikael **Manninen**); 10 March **2005**, Case C-39/04 (Laboratoires **Fournier** SA v Direction des vérifications nationalse et internationales); 5 July 2005, Case C-376/03 (**D.** v Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen); 12 July 2005, Case C-403/03 (Egon **Schempp** v Finanzamt München V); 8 September 2005, Case C-513/03 (J.E.J. **Blanckaert** v Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen); 13 December 2005, Case C-446/03 (**Marks & Spencer** plc v David Halsey (Her Majesty's Inspector of Taxes)); 19 January **2006**, Case C-265/04 (Margaretha **Bouanich** v Skatteverket); 21 February 2006, Case C-152/03 (Hans-Jürgen **Ritter**-Coulais, Monique Ritter-Coulais v Finanzamt Germersheim); 23 February 2006, Case C-253/03 (**CLT-UFA** SA v Finanzamt Köln-West); 23 February 2006, Case C-513/03 (Heirs of M.E.A. **van Hilten**-van der Heijden v Inspecteur van de Belastingdienst/ Particulieren/Ondernemingen buitenland te Heerlen); 23 February 2006, Case C-471/04 (Finanzamt Offenbach am Main-Land v **Keller** Holding GmbH); July 2006, Case C-346/06 (Robert Hans **Conijn** v Finanzamt Hamburg-Nord; 7 September 2006, Case C-470/04 (**N** v Inspecteur van de Belastingdienst Oost/kantoor Almelo); 12 September 2006, Case C-196/04 (**Cadbury Schweppes** plc, Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue); 14 September 2006, Case C-386/04 (Centro di Musicologia Walter **Stauffer** v Finanzamt München für Körperschaften); 3 October 2006, Case C-290/04 (FKP **Scorpio** Konzertproduktionen GmbH v Finanzamt Hamburg-Eimsbüttel); 26 October 2006, Case C-345/05 (**Commission v Portuguese Republic**); 14 November 2006, Case C-513/04 (Mark **Kerckhaert**, Bernadette **Morres** v Belgische Staat); 12 December 2006, Case C-

374/04 (Test Claimants in Class IV of the **ACT Group Litigation** v Commissioners of Inland Revenu); 12 December 2006, Case C-446/04 (Test Claimants in the **FII Group Litigation** v Commissioners of Inland Revenue); 14 December 2006, Case C-170/05 (**Denkavit Internationaal** BV, Denkavit France SARL v Ministre de l'Économie, des Finances et de l'Industrie); 18 January **2007**, Case C-104/06 (**Commission v Sweden**) ; 25 January 2007, Case C-329/05 (Finanzamt Dinslaken v Gerold **Meindl**, Christine Meindl-Berger); 15 February 2007, Case C-345/04 (**Centro Equestre** da Lezíria Grande Lda v Bundesamt für Finanzen); 6 March 2007, Case C-292/04 (Wienand **Meilicke**, Heidi Christa Weyde, Marina Stöffler v Finanzamt Bonn-Innenstadt); 13 March 2007, Case C-524/04 (Test Claimants in the **Thin Cap Group Litigation** v Commissioners of Inland Revenue); 22 March 2007, Case C-383/05 (Raffaele **Talotta** v État belge); 29 March 2007, Case C-347/04 (**Rewe** Zentralfinanz eG v Finanzamt Köln-Mitte); 10 May 2007, Case C-492/04 (**Lasertec** v FA Emmendingen) [order];10 May 2007, Case C-102/05 (Skatteverket v **A and B**) [order] [F]; 24 May 2007, Case C-157/05 (**Holböck** v FA Salzburg-Land); July 2007, Case C-522/04 (**Commission v Belgium**); 18 July 2007, Case C-231/05 (**Oy AA**); 18 July 2007, Case C-182/06 (Grand-duché de Luxembourg v Hans Ulrich **Lakebrink** and Katrin Peters-Lakebrink); 11 October 2007, C-451/05 (**Elisa**); 6 November 2007, Case C-.415/06 (**SWE, Stahlwerk** Ergste Westig GmbH v Finanzamt Dusseldorf-Mettmann) [order]; 8 November 2007, Case C-379/05 (**Amurta** S.G.P.S. v Inspecteur van de Belastingdienst/Amsterdam NL); 6 December 2007, Case C-298/05 (**Columbus** Container Services BVBA v Bielefeld-Innenstadt); 18 December 2007, C-101/05 (**Skatteverket** v A); 18 December 2007, C- 281/06 (Hans-Dieter **Jundt**, Hedwig Jundt v Finanzamt Offenburg); 17 January 2008, Case C-256/06, (Theodor **Jäger** v Finanzamt Kusel-Landstuhl); 17 January 2008, Case C-105/07, (**Lammers & Van Cleeff** v Belgische Staat); 23 April 2008, C-201/05 (The Test Claimants in the CFG v Commissioners of Inland Revenue); 15 May 2008, C-414/06 (Lidl Belgium GmbH & Co. KG v Finanzamt Heilbronn); 20 May 2008, C-194/06 (Staatssecretaris van Financiën v **Orange** European Smallcap Fund NV).

WHO'S AFRAID OF THE *ACTE CLAIR* DOCTRINE?

Daniel Sarmiento

1. The *acte clair* doctrine and the *CILFIT* decision

In 1982 the European Court of Justice (ECJ) introduced a major reform in Art. 234 EC (then Art. 177 EEC) by transforming the obligation of national courts of last instance to make references to the ECJ into a discretionary decision. The Court was importing well-known case law of the French *Conseil d'Etat*, known as the *acte clair* doctrine, whereby national courts could resolve cases of EC law on their own authority when "the correct application of Community law may be so obvious as to leave no scope for any reasonable doubt as to the manner in which the question raised is to be resolved".

This was the contribution of the ECJ in the *CILFIT* case[1], but it was preceded nineteen years earlier by another relevant decision that complements the former. In *Da Costa*[2], the Court exempted national courts of last instance from making references when the case was "materially identical with a question which has already been the subject of a preliminary ruling in a similar case". But while *Da Costa* had introduced an exception to the obligation imposed by Art. 234 EC when the ECJ had previously made a decision on an identical case, the *CILFIT* innovation was much more radical. After all, according to *CILFIT,* national courts of last instance could avoid making the reference even *without* a previous decision from the ECJ, thus transforming them into ultimate arbiters of clear questions of Community law.

The radical appearance of *CILFIT* was fine-tuned by the ECJ in the same judgment, which introduced a series of conditions that national courts were to fulfil before implementing EC law on their own authority. These requirements were supposed to act as a counterbalance to the *acte clair* doctrine, entailing that the national court or tribunal "must be convinced that the matter is equally obvious to the courts of the other member states and to the court of justice"[3], followed by "a comparison of the different language ver-

1. Case 283/81 *CILFIT and Others* [1982] ECR 3415.
2. Joined Cases 28/62 to 30/62 *Da Costa* [1963] ECR 31.
3. *CILFIT*, p. 16.